

# **SDMS US EPA REGION V -1**

**SOME IMAGES WITHIN THIS  
DOCUMENT MAY BE ILLEGIBLE  
DUE TO BAD SOURCE  
DOCUMENTS.**

142134

# 1948

## **ANNUAL REPORT**



---

**NORTH SHORE** *Gas* **COMPANY**

**Waukegan, Illinois**

## 1948 IN BRIEF



### THE YEAR'S GROSS REVENUES

From Sale of Gas.....	\$2,109,928
From Other Gas Revenues.....	27,027
From Interest, Rentals, etc. ....	2,235
	<u>\$2,139,190</u>

### THE YEAR'S EXPENSES AND APPROPRIATIONS

To Serve 30,700 Utility Customers

#### For Employee Services

Operating Payrolls .....	\$ 548,522
<i>Average Number of Operating Employees—205</i>	
Social Security Taxes.....	7,795
<i>Company Payments Toward Federal Pensions and Unemployment Insurance</i>	
Insurance .....	5,338
<i>Portion of Employees' Group Insurance Paid by the Company</i>	
	<u>\$ 561,655</u>

#### For Other Operation and Maintenance Expense

Cost of Gas Purchased for Resale.....	\$ 366,226
<i>2,724,980 M.C.F. of Gas Purchased (average 1,045 Btu)</i>	
Other Materials, Supplies, and Expenses.....	101,901
<i>A Multiplicity of Items Needed to Run the System</i>	
Property Losses Chargeable to Operations.....	229,694
<i>Amortization of Loss on Sale of Coke Oven Plant</i>	
For Future Retirement of Property.....	131,728
<i>Wear and Tear and Obsolescence of Properties</i>	
Miscellaneous .....	67,934
<i>Including Conversion Expense and Miscellaneous Interest Payments</i>	
	<u>\$ 897,483</u>

#### Required for Government

State, Local, and Miscellaneous Taxes (Excluding Social Security Taxes).....	\$ 119,396
<i>Mostly Real Estate and Personal Property</i>	
Federal Income Taxes—After Applying \$187,446 Against the Coke Oven Plant Sale Loss.....	59,645
	<u>\$ 179,041</u>

#### For Use of Security Holders' Money

Interest on Mortgage Bonds.....	\$ 130,433
<i>\$3,069,000 Outstanding at Year End</i>	
Dividend to Shareholders of \$1.35 per Share.....	181,379
<i>134,355 Shares Held by 2,061 Shareholders at Year End</i>	
	<u>\$ 311,812</u>

#### Money Left in the Business

Amount Remaining After All Expenses and Appropriations.....	\$ 189,199
<i>Needed for Expansion of Service to Customers and Other Corporate Purposes</i>	
	<u>\$2,139,190</u>

## FINANCIAL OPERATIONS



*Revenues and Expenses:* The following discussion relates to the more important items of our Income Accounts on page 12:

Gross revenues for 1948 were \$2,136,955, an increase of \$259,992, or 14%, over 1947. The increase in revenues was accompanied by a \$77,663 rise in total expenses (including all taxes). Operating expenses for 1948 were \$1,768,612. Increases by classes of expense are explained below.

The cost of gas purchased plus the cost of standby operation at our production plants amounted to \$430,488, which was \$49,727 below the comparative figure for the year 1947, even though the gas sendout was 50% higher in 1948 than in 1947. This decrease in gross cost resulted from the low unit cost of purchased gas compared to the high unit cost of manufactured gas, which had been used exclusively in the first seven months of 1947.

The Board of Directors recently determined that beginning with the year 1949, the Company's annual provision for depreciation of its properties should be at the rate of 2½% of depreciable property. For 1948 and prior years, the annual provision has been equal to \$35,000 plus 1.75% of net additions to property since January 1, 1921. If the new policy had been in effect in 1948, the provision for depreciation would have been approximately \$176,400 instead of \$131,728.

In last year's report we explained that, in connection with the changeover from manufactured to natural gas in 1947, the Company expended certain moneys to convert customers' facilities to use natural gas efficiently. We also stated that as soon as natural gas was made available to the Company's customers, its coke oven plant was sold at a loss of \$1,502,182, and that this loss, to the extent allowable for Federal income tax purposes, might be applied against otherwise taxable income for 1947 and the two preceding and two succeeding years, and we anticipated this would result in the recovery, elimination, and reduction of Federal income taxes to the extent of \$421,870. On December 12, 1947, the Illinois Commerce Commission ordered in effect that the Federal income tax savings be applied against the loss, and in addition that the Company write-off \$657,828 of the loss against capital surplus. The balance of \$422,484 was to be amortized against income over a period of ten years beginning July 1, 1947.

During 1948, a full year's write-off of the unamortized balance of the cost of converting customers' facilities to natural gas and the loss suffered in the

sale of the coke oven plant, amounting to \$56,184 and \$42,248, respectively, was charged against operations. During 1947, the amounts so written-off were \$28,200 and \$21,124, respectively.

As a result of the loss on the sale of the coke oven plant and the related effect upon 1945-1946 Federal income taxes, the Company received \$116,966 during the year as a refund of tax payments for those years. Further, the tax on otherwise taxable income for 1947, amounting to \$117,458, was entirely eliminated, and a savings of \$187,466 was made on this year's tax, completing the total amount of savings. After the savings mentioned above, it was necessary to provide only \$59,645 for 1948 Federal income tax.

*Earned Surplus:* Net income of \$370,578 was carried to earned surplus.

During the year we paid two dividends, each of 50 cents per share in cash, and on December 20, declared another dividend of 35 cents per share, to be paid in cash on January 15, 1949. These dividends were charged against earned surplus.

*Assets:* During 1948 the Company expended \$460,831 in its construction program. We removed \$27,670 of property and equipment from service. This left \$433,161 net increase in our property and plant investment.

The cash on hand increased during the year by \$105,615, and our stocks of construction and maintenance materials were up \$107,610.

The unamortized balances of the loss on sale of coke oven plant and natural gas conversion expense were reduced by charges against operations of \$98,432, refund of \$2,070 from contractor after audit of conversion expenses, and savings of \$187,446 in Federal income taxes.

*Liabilities:* A bank loan in the amount of \$200,000 was paid off during the year, and there are no bank loans now outstanding.

Because the sinking fund provision of the mortgage indenture becomes effective in 1949, an amount of \$76,000 has been moved from long term debt and included in current liabilities due within one year.

The dividend declared on December 20, of 35 cents per share, amounting to \$47,024, and the amount provided for Federal tax due on 1948 income, amounting to \$59,645, are reflected as increases in current liabilities over those of 1947.

The balance in depreciation reserve at the year-end was \$2,156,519, or 29% of depreciable property. This was an increase of \$130,655 for the year.



# INCOME ACCOUNTS



FOR THE YEARS ENDED DECEMBER 31, 1948 AND 1947

	<u>1948</u>	<u>1947</u>
Operating revenues:		
Gas sales .....	\$2,109,928	1,852,054
Other gas revenues .....	27,027	24,909
	<u>\$2,136,955</u>	<u>1,876,963</u>
Operating revenue deductions:		
Manufactured gas production—		
Operation .....	\$ 54,109	950,226
Maintenance .....	10,153	27,624
Credit for residuals (by-products) .....	—	(623,197)
	<u>\$ 64,262</u>	<u>354,653</u>
Gas purchased .....	366,226	125,562
Other operating expenses—		
Operation (including amortization of natural gas conversion expenses, 1948—\$56,183.64; 1947—\$28,200.81) (Note 1) .....	577,699	545,433
Maintenance .....	69,984	71,962
Provision for depreciation (Note 2) .....	131,728	156,483
Amortization of loss on sale of coke oven plant (Note 1) .....	42,248	21,124
Taxes (other than Federal income taxes) .....	127,191	134,435
	<u>\$1,379,338</u>	<u>1,409,652</u>
Operating income .....	\$ 757,617	467,311
Other income .....	2,235	1,249
Gross income .....	<u>\$ 759,852</u>	<u>468,560</u>
Income deductions:		
Interest on long-term debt .....	\$ 130,433	151,514
Amortization of debt discount and expense .....	5,513	5,513
Other interest charges .....	6,237	6,812
	<u>\$ 142,183</u>	<u>163,839</u>
	<u>\$ 617,669</u>	<u>304,721</u>
Federal income taxes and other charges:		
Provision for Federal income taxes .....	\$ 59,645	—
Amortization of loss on sale of coke oven plant to extent of Federal income taxes eliminated thereby (Note 1) .....	187,446	117,458
	<u>\$ 247,091</u>	<u>117,458</u>
Net income for the year .....	<u><u>\$ 370,578</u></u>	<u><u>187,263</u></u>

See accompanying notes.

1947 ANNUAL REPORT  
OF  
NORTH SHORE GAS COMPANY

Waukegan, Illinois

March 15, 1948

*To the Shareholders of  
North Shore Gas Company:*

The year 1947 was a most eventful one for the Company.

The following paragraph is taken from the "Balance Sheet" comments which will be found on page 12. It is indicative of the progress that has taken place since the Company changed from manufactured gas to natural gas:

Net income for 1947 in the amount of \$187,263 was carried to earned surplus. This amounted to \$1.39 per share on 134,355 shares of common stock outstanding. Dividends aggregating 50-cents per share were declared and paid during the year.

In the reports of the last two years you were informed of the plans of the Company to change its product from a manufactured gas, having a heating value of approximately 565 Btu per cubic foot, to (a 1,040 Btu per cubic foot) natural gas, and to supplement the natural gas, should an emergency arise, with certain liquified petroleum air gas and high Btu carbureted water gas. A new schedule of lower rates was to be put into effect at the time of the introduction of natural gas.

In the year 1947, this goal was reached with the introduction of straight natural gas into the Company's distribution system on May 12. By July 21, the customers of the Company were being served with natural gas purchased from and transported by the Natural Gas Pipeline Company of America, from the great natural gas fields of the Southwest.

During the period beginning with the introduction of natural gas, and until every customer of the Company had been thus served, approximately 90,000 appliances of these customers were converted to use natural gas by the Conversions & Surveys, Inc., a company specializing in this type of work.

On June 22, the Company had used the last of its coal at the coke oven plant, and made ready to abandon this facility, however, negotiations which had been under way materialized, and the Waukegan Coke Corporation, on June 25, signed a contract to purchase the coke oven plant for a cash consideration of \$650,000.00. The sale was consummated on July 14, and the cash received was deposited with the Trustee, under the mortgage indenture, who subsequently on October 14, redeemed \$631,000.00 principal amount of the First Mortgage 4 $\frac{1}{4}$ % Bonds, Series A, at a price of 103 per cent of the par value.

The sale of the coke oven plant resulted in a book loss of \$1,502,182.14. This loss, to the extent allowable for Federal income tax purposes, may be applied against otherwise taxable income for 1947 and the two preceding and two succeeding years and, it is anticipated, will result in the recovery, elimination and reduction of Federal income taxes to the extent of \$421,869.21. On December 12, 1947, the Illinois Commerce Commission ordered (Docket #35705), in effect, (1) that anticipated recoveries of Federal income taxes paid for 1945 and 1946, in the amount of \$116,965.80 be applied against the loss, (2) that \$657,828.36 of the loss be written off and charged to capital surplus that was set up at the time of the acquisition of the coke oven plant in 1941 through the issuance of 57,041 common shares and the assumption of certain liabilities, (3) that the loss be amortized against income for the years 1947, 1948, and 1949 to the extent of Federal income tax savings resulting from the loss, which savings were estimated to aggregate \$304,903.41, and (4) that the remaining loss, estimated to be \$422,484.57, be amortized against income over a period of ten years beginning July 1, 1947 in substantially equal amounts of approximately \$42,248.46.

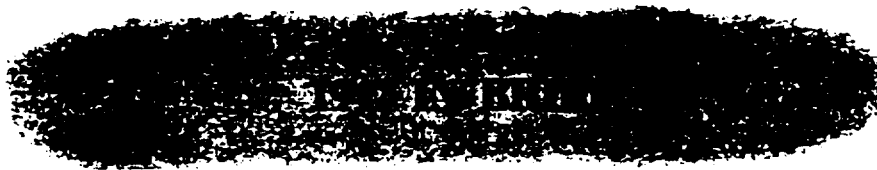
With the introduction of natural gas into the Company's distribution system, the discontinuance of the manufacture of coal gas, and the subsequent sale of the coke oven plant, the Company, in order to have certain standby facilities in case of an emergency converted its water gas manufacturing set at the North Plant in Waukegan so it would have a daily manufacturing capacity of 2,500 M.C.F. of high (1,000) Btu carbureted water gas, and, in addition, completed the installation of two units for the manufacture of liquified petroleum-air gas, each with a daily capacity of 5,000 M.C.F. of 1,230 Btu gas. One of these units was installed at the North Plant in Waukegan, at one end of the system, and the other at the Deerfield Pumping Station, at the other end of the system.

Along with the introduction of natural gas, the Company promulgated lower rate schedules. These new reduced rates effected a savings to our customers of approximately

\$238,000.00 on an annual basis; however, an aggressive new business and merchandising program has already shown good results, so that this loss in revenue will be recouped in a comparatively short time.

The following pages present for your information important details of the year's operations.

The financial and statistical statements, and the independent auditor's certificate are given at the end of the text beginning on page 22.



### THE YEAR'S GROSS REVENUES

From Sale of Gas and Steam.....	\$1,876,963
From Interest, Rentals, etc.....	1,249
	<u>\$1,878,212</u>

### THE YEAR'S EXPENSES AND APPROPRIATIONS

#### To Serve 29,600 Utility Customers

##### For Employee Services

Operating Payrolls .....	\$ 659,911
Average Number of Operating Employees—234	
Social Security Taxes .....	10,060
Company Payments Toward Federal Pensions and Unemployment Insurance	
Insurance .....	7,416
Portion of Employees' Group Insurance Paid by the Company	
	<u>\$ 677,387</u>

##### For Other Operation and Maintenance Expenses

Cost of Coal Carbonized (Six Months Operation of Coke Plant) .....	\$ 499,717
76,400 Tons of Coal Carbonized	
Cost of Fuel for Boilers and Gas Producer Plant.....	153,827
30,495 Tons Burned	
Cost of Gas Purchased for Resale.....	125,562
1,055,258 M.C.F. of Gas Purchased in Addition to the	
1,289,237 M.C.F. of Gas Manufactured in First 6 Months	
Other Materials, Supplies, and Expenses .....	246,174
A Multiplicity of Items Needed to Run the System	
Property Losses Chargeable to Operations.....	138,582
Amortization of Loss on Sale of Coke Oven Plant	
For Future Retirement of Property.....	156,483
Wear and Tear and Obsolescence of Properties	
Miscellaneous .....	40,525
Including Conversion Expense and Miscellaneous Interest Payments	
Production Expense Credits—Residuals.....	(623,197)
Received in Disposition of By-Products of Gas Manufacture	
	<u>\$ 737,673</u>

##### Required for Government

State, Local, and Miscellaneous Taxes (Excluding Social Security Taxes) .....	\$ 124,375
Mostly Real Estate and Personal Property	
Federal Income Taxes of \$117,458—Applied Against the Coke Plant Sale Loss.....	—
	<u>\$ 124,375</u>

##### For Use of Security Holders' Money

Interest on Mortgage Bonds.....	\$ 151,514
\$3,069,000 Outstanding at Year End	
Dividend to Shareholders of 50-Cents per Share.....	67,177
134,355 Shares Held by 2,144 Shareholders at Year End	
	<u>\$ 218,691</u>

##### Money Left in the Business

Amount Remaining After All Expenses and Appropriations.....	\$ 120,086
Needed for Expansion of Service to Customers and Other Corporate Purposes	
	<u>\$1,878,212</u>

# NORTH SHORE GAS COMPANY

## BALANCE SHEETS — DECEMBER 31, 1947 AND 1946

### ASSETS AND DEFERRED CHARGES

	Dec. 31, 1947	Dec. 31, 1946
<b>Utility Plant (Note 2):</b>		
Franchises, organization expense, etc. ....	\$ 137,031.65	140,520.50
Gas plant .....	7,134,204.35	10,065,830.77
	<u>\$ 7,271,236.00</u>	<u>10,206,351.27</u>
<b>Current Assets:</b>		
Cash in banks and on hand .....	\$ 492,117.68	643,094.27
U. S. War Savings bonds, at cost .....	3,700.00	3,700.00
Accounts receivable, less reserves of \$15,188.84 and \$15,398.34, respectively, for uncollectible accounts .....	136,107.73	146,418.81
Claims for refund of Federal income taxes paid for 1945 and 1946 (Note 1) ..	116,965.80	
<b>Inventories—</b>		
Coal for carbonization, at cost .....		415,877.01
Operating and construction materials and supplies, at cost .....	146,334.55	92,189.29
Merchandise for resale, at cost .....	72,808.03	18,439.62
Residual products, at values substantially less than selling prices .....	2,420.22	12,828.79
	<u>\$ 970,454.01</u>	<u>1,332,547.79</u>
<b>Other Assets:</b>		
Physical property, other than utility plant, at cost .....	\$ 41,193.25	41,193.25
Miscellaneous securities, at cost .....	980.00	980.00
Special deposits .....	1,809.48	1,639.48
	<u>\$ 43,982.73</u>	<u>43,812.73</u>
<b>Deferred Charges:</b>		
Unexpired insurance and prepaid taxes .....	\$ 8,823.56	14,149.43
Unamortized debt discount and expense .....	65,088.13	70,601.38
Leasehold improvements in process of amortization over terms of leases .....	13,016.26	2,658.16
Loss on sale of coke oven plant, in process of amortization (Note 1) .....	588,805.91	
Natural gas conversion expenses, in process of amortization (Note 1) .....	535,815.35	48,619.96
Miscellaneous .....	8,133.24	6,831.90
	<u>\$ 1,219,682.45</u>	<u>142,860.83</u>
	<u>\$ 9,505,355.19</u>	<u>11,725,572.62</u>

(See accompanying notes)

**NORTH SHORE *Gas* COMPANY**

**Annual Report  
to Shareholders**

**1946**

# NORTH SHORE GAS COMPANY

BALANCE SHEETS — DECEMBER 31, 1946 and 1945  
(See Accompanying Notes)

## ASSETS AND DEFERRED CHARGES

	December 31, 1946	December 31, 1945
<b>Utility Plant:</b>		
Franchises, organization expense, etc.....	\$ 140,520.50	\$ 140,520.50
Gas plant.....	10,065,830.77	9,663,564.00
	<u>\$10,206,351.27</u>	<u>\$ 9,804,084.50</u>
 <b>Current Assets:</b>		
Cash in banks and on hand.....	\$ 643,094.27	\$ 602,650.81
U. S. certificates of indebtedness, war savings bonds and stamps.....	3,700.00	403,825.00
Accounts receivable, less reserves of \$15,398.34 and \$16,509.07, respectively, for uncollectible accounts.....	146,418.81	163,489.62
Interest receivable.....		293.27
<b>Inventories:</b>		
Coal for carbonization, at cost.....	415,877.01	317,700.22
Operating and construction materials and supplies, at cost.....	92,189.29	98,373.31
Merchandise for resale, at cost.....	18,439.62	8,951.49
Coke and other residual products, at values substantially less than selling prices, less selling expenses.....	12,828.79	51,642.03
	<u>\$ 1,332,547.79</u>	<u>\$ 1,646,925.75</u>
 <b>Other Assets:</b>		
Physical property, other than utility plant.....	\$ 41,193.25	
Miscellaneous securities, at cost.....	980.00	980.00
Appliances installed in customers' premises under rental purchase contracts.....		49.42
Special deposits.....	1,639.48	21,839.66
	<u>\$ 43,812.73</u>	<u>\$ 22,869.08</u>
 <b>Deferred Charges:</b>		
Unexpired insurance and prepaid taxes.....	\$ 14,149.43	\$ 5,343.54
Unamortized debt discount and expense.....	70,601.38	78,285.29
Leasehold improvements in process of amortization over term of lease.....	2,658.16	3,517.84
Natural gas conversion expenses, tools, materials and supplies, less \$7,551.39 written off against income.....	48,619.96	
Miscellaneous .....	6,831.90	5,740.05
	<u>\$ 142,860.83</u>	<u>\$ 92,886.72</u>
	<u>\$11,725,572.62</u>	<u>\$11,566,766.05</u>



## 1946 IN BRIEF

### THE YEAR'S GROSS EARNINGS

From Sale of Gas and Steam.....	\$1,834,341
From Interest, Rentals, etc.....	804
	<hr/>
	\$1,835,145

### THE YEAR'S EXPENSES AND APPROPRIATIONS

#### To Give Service to 29,000 Utility Customers For Employees

Payrolls .....	\$ 698,554
Average Number of Operating Employees—266	
Social Security Taxes.....	11,349
Company Payments Towards Federal Pensions and Unemployment Insurance	
Insurance.....	8,174
	<hr/>
	\$ 718,077

#### For Other Operation and Maintenance Expenses

Cost of Coal for Carbonization.....	\$1,011,036
155,192 Tons of Coal Carbonized	
Cost of Fuel for Boilers and Gas Producer Plant.....	226,585
53,510 Tons Burned	
Other Materials, Supplies, and Expenses.....	387,608
A Multiplicity of Things Needed to Run the System	
For Future Retirements of Property.....	182,058
Wear and Tear and Obsolescence of Properties	
Production Expense Credits—Residuals.....	(1,176,920)
Received in Disposition of By-Products of Gas Manufacture	
	<hr/>
	\$ 630,367

#### Required for Government

State, Local, and Miscellaneous Taxes (Excluding Social Security Taxes).....	\$ 151,785
Mostly Real Estate and Personal Property Taxes	
Federal Income Taxes.....	57,054
Represents Estimated Income Tax Liability for the Year	
	<hr/>
	\$ 208,839

#### For Bond and Note Holders

Interest on Mortgage Bonds.....	\$ 157,250
\$3,700,000 Outstanding at Year End	
Interest on Serial Notes.....	7,667
None Outstanding at Year End	
	<hr/>
	\$ 164,917

#### For Stockholders

Net Income Available for Dividends and Earned Surplus \$.84 per Share.....	\$ 112,945
(Dividends of \$.50 per Share Paid \$67,127)	
	<hr/>
	\$1,835,145

NOTE: Please refer to the text of this report for explanation of various items in this statement.

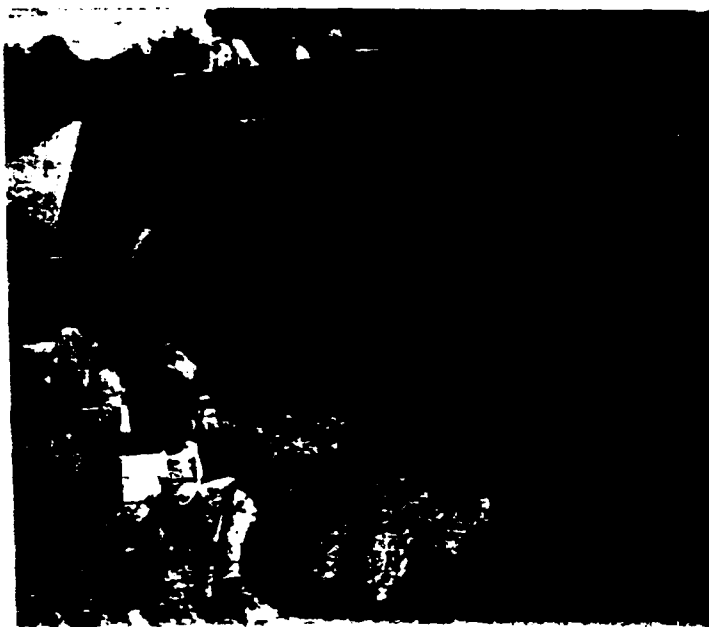


There was an increase of \$170,825 during the year in retirement (depreciation) reserve. Total appropriations to the reserve aggregated \$187,587, consisting of charges to operating expenses of \$182,058 and charges to other accounts of \$5,529. Net write-offs against the reserve amounted to \$16,762, this being the cost of property retired during the year less the net value of salvage material.

### Natural Gas

IN the 1945 annual report you were informed that the Illinois Commerce Commission had on January 8, 1946, issued an order authorizing your Company to change the type and heating value of the gas then being served, i.e., from manufactured gas having a heating value of 565 B.T.U. per cubic foot to straight natural gas having a heating value of approximately 1,000 B.T.U. per cubic foot. The

### IS PIPELINE CONNECTION



order of the Commission also approved a new schedule of lower rates to be applied to the use of the straight natural gas when introduced. The order authorized the Company to convert the customers' appliances so that they could utilize the new straight natural gas and provides that the total cost of the conversion expense shall be borne by the Company. A certificate of convenience and necessity was also issued by the Commission authorizing the Company to construct, maintain and operate certain facilities, for a connection with the pipeline of the Natural Gas Pipeline Company of America, from whom the gas for resale would be purchased. The Commission authorized the abandonment of the Company's Coke Oven Plant, and recovery of the undepreciated cost on a plan of amortization against earnings over a period of years, but the manner and details of said plan of amortization are to be covered in a subsequent order.

The Natural Gas Pipeline Company of America, under date of May 10, 1946, obtained a certificate of convenience and necessity to serve our Company with natural gas, and it was our hope that the changeover from manufactured gas to natural gas might be completed before the 1946 year-end. Your Company completed its construction for the connection facilities in the fall of 1946, but these facilities were not placed in operation due to difficulties encountered by the pipeline company in procuring its pipe and fittings, the installation of which is necessary before the physical connection can be made to turn gas into our distribution system. This delay has postponed the connection to natural gas until about April 1, 1947.

The Company has contracted with Conversions & Surveys, Inc., a corporation engaged in changeover work, to do all the necessary work to convert our customers' appliances to utilize straight natural gas. This work will be started as soon as the gas begins to flow into our distribution system, and should be completed by the end of June. It appears at the present time that June will be the last month of manufacturing gas and by-products at the Coke Oven Plant. If the changeover schedule as outlined is adhered to, the abandonment of the Coke Oven Plant should come during the month of July. The Company has engaged L. J. Sheridan & Company, of Chicago, industrial real estate brokers, to assist it in disposal of the Coke Plant site.

It is estimated after full conversion to natural gas about July 1, the new rates will result in a reduction of charges for gas service to our 29,000 customers of approximately an annual figure of \$238,000.

Forecasts today must be tempered by economic uncertainties, but with the lower rates and the anticipated large volume of residential and commercial building, it is the Company's expectation, based on experiences of other gas companies in the changeover from manufactured gas to natural gas service, that revenues lost through reduced rates will be recouped in a comparatively short time.

**NORTH SHORE** *Gas* **COMPANY**

**Annual Report  
to Shareholders**

**1945**

## RESULTS FOR 1945

### THE YEAR'S GROSS EARNINGS

From Sale of Gas and Steam.....	\$1,799,028
From Interest, Rentals, etc.....	4,376
	\$1,803,404

### THE YEAR'S EXPENSES AND APPROPRIATIONS

*To Give Service to 29,000 Utility Customers*

#### For Employees

Payrolls.....	\$ 606,112
<i>Average Number of Operating Employees—237</i>	
Social Security Taxes.....	10,068
<i>Company Payments Towards Federal Pensions and Unemployment Insurance</i>	
Insurance.....	6,356
<i>Portion of Employees' Insurance Paid by the Company</i>	

\$ 622,536

#### For Other Operation and Maintenance Expenses

Cost of Coal for Carbonization.....	\$ 948,240
<i>160,386 Tons of Coal Carbonized</i>	
Cost of Fuel for Boilers and Gas Producer Plant.....	237,564
<i>49,187 Tons Burned</i>	
Other Materials, Supplies, and Expenses.....	370,268
<i>A Multiplicity of Things Needed to Run the System</i>	
For Future Retirements of Property.....	180,701
<i>Wear and Tear and Obsolescence of Properties</i>	
Production Expense Credits—Residuals.....	(1,104,556)
<i>Received in Disposition of By-Products of Gas Manufacture</i>	

\$ 632,217

#### Required for Government

State, Local, and Miscellaneous Taxes (Excluding Social Security Taxes).....	\$ 156,944
<i>Mostly Real Estate and Personal Property Taxes</i>	
Federal Income Taxes.....	79,853
<i>Normal and Surtax to be Paid on 1945 Net Income</i>	

\$ 236,797

#### For Security Holders

Interest on Mortgage Bonds.....	\$ 157,250
<i>\$3,700,000 Outstanding at Year End</i>	
Interest on Serial Notes.....	13,333
<i>\$300,000 Outstanding at Year End</i>	
Dividends to Stockholders.....	67,177
<i>50c per Share on 134,355 Shares Outstanding (\$15 Par)</i>	

\$ 237,760

<b>TOTAL YEAR'S EXPENSES, TAXES, INTEREST, AND DIVIDENDS.....</b>	<b>\$1,729,310</b>
Additions to Earned Surplus.....	74,094
<i>Amount remaining after year's expenses and appropriations</i>	

\$1,803,404

This statement should be considered in connection with the text and statements at the end of this report.

The Company has renewed its union agreement. Formerly the hourly paid employees had been represented by two locals of the same union. During 1945 the two locals were consolidated into one.

### Natural Gas

IN our 1944 annual report we stated that your Company had retained the Stone & Webster Service Corporation to make a study of the possibilities of the Company utilizing natural gas in conjunction with its manufactured gas for distribution to its customers. The report on this study concluded that it would be more advantageous to the Company and its customers to distribute straight natural gas rather than a mixture of manufactured and natural gas. Upon the basis of that report and the recommendation of the operating management the Board of Directors authorized a petition to the Illinois Commerce Commission for approval to change the type and heating value of the gas now served, i.e., from manufactured gas having a heating value of 565 B.T.U. per cubic foot to straight natural gas having a heating value of approximately 1,000 B.T.U. per cubic foot. After hearings an order approving the change was entered on January 8, 1946. The order of the Commission also approved a new schedule of lower rates proposed by the Company for introduction with the use of straight natural gas. The new schedule will amount to a reduction of approximately 14% to the customer. The introduction of straight natural gas will require the expenditure of substantial amounts for change-over expenses, estimated at \$225,000, and an additional substantial amount for enlargement of distribution facilities.



It is proposed to purchase the Company's gas requirements from the Natural Gas Pipeline Company of America. That Company made application to the Federal Power Commission for a certificate of convenience and necessity to extend and enlarge its system so that our requirements for gas, as well as others, may be served. The hearing on that application was begun on January 14, 1946. It is hoped that approval will be granted in time for change over before the next winter season.

### Franchises

**Franchises:** The Company sought and received two new five year franchises from the City of Lake Forest and Village of Lake Bluff, and one new ten year franchise from the City of Highwood.

### Directors and Officers

At the annual shareholders meeting held in April, 1945, Mr. Sydney K. Schiff, a partner of Pam. Hurd & Reichmann, attorneys-at-law, Chicago, Illinois, was elected a Director and subsequently Chairman of the Board.

### Conclusion

**I**N the year 1945 your Company handled the largest volume of business in its history. The Board of Directors compliments all officers and employees for their fine performance, under abnormal wartime and unstable conditions, in the interest of shareholders, employees, and customers.

By order of the Board of Directors.

A. W. CONOVER,  
*President and General Manager.*

SYDNEY K. SCHIFF,  
*Chairman*



# NORTH SHORE GAS COMPANY

## INCOME ACCOUNTS

FOR THE YEARS ENDED DECEMBER 31, 1945 AND 1944  
(See Accompanying Notes)

	1945	1944
Operating Revenues:		
Gas sales.....	\$ 1,777,092.72	\$ 1,720,332.37
Other gas revenues.....	21,935.30	32,022.14
	<u>\$1,799,028.02</u>	<u>\$1,752,354.51</u>
Operating Revenue Deductions:		
Manufactured gas production—		
Operation .....	\$ 1,623,122.17	\$ 1,549,519.13
Maintenance .....	52,667.02	61,976.11
Credit for residuals (by products).....	—1,104,556.01	—1,137,526.25
	<u>\$ 571,233.18</u>	<u>\$ 473,968.99</u>
Other operating expenses—		
Operation .....	424,175.06	411,408.29
Maintenance .....	58,357.27	61,963.18
Provision for depreciation and/or retirements.....	180,700.99	179,827.13
Taxes (other than federal income taxes).....	167,011.95	167,459.29
	<u>\$1,401,478.45</u>	<u>\$1,294,626.88</u>
Operating Income.....	<u>\$ 397,549.57</u>	<u>\$ 457,727.63</u>
Other Income.....	4,376.34	5,322.19
Gross Income.....	<u>\$ 401,925.91</u>	<u>\$ 463,049.82</u>
Income Deductions:		
Interest on long-term debt.....	\$ 170,583.30	\$ 173,750.00
Amortization of debt discount and expense.....	7,105.06	7,539.20
Other interest charges.....	3,112.82	2,848.30
	<u>\$ 180,801.18</u>	<u>\$ 184,137.50</u>
	<u>\$ 221,124.73</u>	<u>\$ 278,912.32</u>
Federal Income Taxes and Portion of Loss on Sale of Real Estate:		
Provision for Federal Income Taxes (no excess profits Taxes are anticipated).....	\$ 67,422.90	\$ 100,989.68
Portion of Loss on Sale of Real Estate Equal to Federal Income Tax Reduction Resulting Therefrom (balance of loss Charged to Earned Surplus).....	12,430.45	100,989.68
	<u>\$ 79,853.35</u>	<u>\$ 100,989.68</u>
Net Income for the Year.....	<u>\$ 141,271.38</u>	<u>\$ 177,922.64</u>

## SURPLUS ACCOUNTS

FOR THE YEAR ENDED DECEMBER 31, 1945  
(See Accompanying Notes)

### EARNED SURPLUS SINCE MAY 31, 1941

Balance, December 31, 1944.....		\$ 470,340.74
Net income for the year ended December 31, 1945.....		141,271.38
		<u>\$ 611,612.12</u>
Dividends paid in cash on common stock—\$.50 per share .....		67,177.50
		<u>\$ 544,434.62</u>
Loss on sale of real estate.....	\$ 31,076.12	
Less: Portion thereof (equal to federal income tax reduction resulting from such loss) charged against income.....	12,430.45	
		<u>18,645.67</u>
Balance, December 31, 1945.....		<u>\$ 533,788.95</u>

### CAPITAL SURPLUS

Balance, December 31, 1944.....	\$1,756,854.70
Balance, December 31, 1945.....	<u>1,756,854.70</u>



**NORTH SHORE *Gas* COMPANY**

**Annual Report  
to Shareholders**

**1944**

**NORTH SHORE GAS COMPANY**  
**BALANCE SHEETS — DECEMBER 31, 1944 and 1943**  
(See Accompanying Notes)

**ASSETS AND DEFERRED CHARGES**

	December 31, 1944	December 31, 1943
<b>Utility Plant:</b>		
Franchises, organization expense, etc.....	\$ 140,520.50	\$ 140,520.50
Gas plant.....	9,637,002.19	9,576,487.04
	<b>\$ 9,777,522.69</b>	<b>\$ 9,717,007.54</b>
 <b>Current Assets:</b>		
Cash in banks and on hand.....	\$ 312,275.08	\$ 544,669.30
U. S. certificates of indebtedness, war savings bonds and stamps.....	453,825.00	3,840.00
Accounts receivable, less reserves of \$17,854.37 and \$19,862.29, respectively, for uncollectible accounts.....	143,642.01	164,943.33
Interest receivable.....	912.06	
<b>Inventories:</b>		
Coal for carbonization, at cost.....	365,489.67	401,252.00
Operating and construction materials and supplies, at cost.....	110,494.45	115,275.02
Merchandise for resale, at cost.....	7,739.49	4,469.59
Coke and other residual products, at values substantially less than selling prices, less selling expenses.....	59,206.50	66,579.67
	<b>\$ 1,453,584.26</b>	<b>\$ 1,301,028.91</b>
 <b>Other Assets:</b>		
Miscellaneous securities, at cost.....	\$ 980.00	\$ 980.00
Appliances installed in customers' premises under rental purchase contracts.....	723.61	3,223.10
Special deposits.....	1,833.46	1,833.46
	<b>\$ 3,337.07</b>	<b>\$ 6,036.56</b>
 <b>Deferred Charges:</b>		
Unexpired insurance and prepaid taxes.....	\$ 10,349.81	\$ 16,641.37
Unamortized debt discount and expense.....	85,390.35	92,929.55
Leasehold improvements in process of amortization over term of lease.....	4,377.52	5,237.20
Miscellaneous.....	8,773.17	10,822.60
	<b>\$ 108,890.85</b>	<b>\$ 125,630.72</b>
	<b><u>\$11,343,534.87</u></b>	<b><u>\$11,149,703.73</u></b>

# EXPLANATORY EARNINGS AND EXPENSE STATEMENT FOR 1944

## THE YEAR'S GROSS EARNINGS

From Sale of Gas and Steam .....	\$1,752,354
From Other Sources, Such as Interest, Dividends, and Rentals of Company Property .....	5,322
	<u>\$1,757,676</u>

## THE YEAR'S EXPENSES AND APPROPRIATIONS

To Give Service to 29,000 Utility Customers

### For Employees

Payrolls .....	\$ 581,277
239 Operating Employees at Year End	
Social Security Taxes .....	9,765
Company Payments Towards Federal Pensions and Unemployment Insurance	
Insurance .....	5,302
Portion of Employees' Insurance Paid by the Company	
	<u>\$ 596,344</u>

### For Other Operation and Maintenance Expenses

Cost of Coal for Carbonization .....	\$ 931,330
162,774 Tons of Coal Carbonized	
Cost of Fuel for Boilers and Gas Producer Plant .....	223,477
46,338 Tons Burned	
Other Materials, Supplies, and Expenses .....	353,868
A Multitude of Things Needed to Run the System	
For Future Retirements of Property .....	179,827
Wear and Tear and Obsolescence of Properties	
Production Expense Credits—Residuals .....	(1,137,526)
Received in Disposition of By-Products of Gas Manufacture	
	<u>\$ 550,976</u>

### Required for Government

State, Local, and Miscellaneous Taxes (Excluding Social Security Taxes) .....	\$ 157,694
Mostly Real Estate and Personal Property Taxes	
Federal Income Taxes .....	100,990
Normal and Surtax to be Paid on 1944 Net Income	
	<u>\$ 258,684</u>

### For Security Holders

Interest on Mortgage Bonds .....	\$ 157,250
\$3,700,000 Outstanding at Year End	
Interest on Serial Notes .....	16,500
\$400,000 Outstanding at Year End	
Dividends to Stockholders .....	67,177
50¢ per Share on 134,355 Shares Outstanding (\$15 Par)	
	<u>\$ 240,927</u>

<b>TOTAL YEAR'S EXPENSES, TAXES, INTEREST, AND DIVIDENDS .....</b>	<b>\$1,646,931</b>
Addition to Earned Surplus .....	110,745
Amount remaining after year's expenses and appropriations	
	<u>\$1,757,676</u>

This statement should be considered in connection with the text and statements at the end of this report.



## North Shore Goes "Natural"

Illinois utility speeds changeover with  
everything from jeep to portable shop

I HAVE dreamed of these valves for five years," sighed A. W. Conover, president, North Shore Gas Co., Waukegan, just before natural gas was turned on for 30,000 customers in northeastern Illinois. With Mr. Conover were C. J. Mulholland, secretary-treasurer, and William Wuestenfeld, general superintendent of distribution (top photo at right).

During the changeover from manufactured to natural gas an \$8 million portable shop was used to service 200 appliance adjusters (side and rear views shown at right). A new jeep ditcher proved invaluable, digging ditches up to 300 feet an hour (see above).

Numerous improvements were made. An attractive window display stressed the theme, "It's the flame that makes it perfect." The utility's Libertyville office and store were remodeled (lower right) and a cashier's desk added of original design that has proved popular with customers and cashier alike. Above the door a sign announces "Natural Gas Will Soon Be Here."

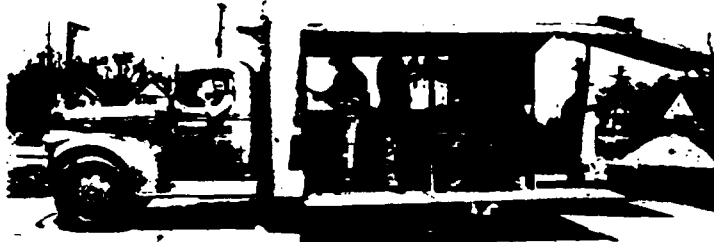


Exhibit U

O P I N I O N  
OF  
HALL & HULSE  
COVERING TITLE TO REAL ESTATE  
OF  
NORTH SHORE COKE & CHEMICAL COMPANY

ALBERT L. HALL  
MINARD E. HULSE  
HARRY A. HALL  
MARSHALL MEYER

LAW OFFICES  
**HALL AND HULSE**  
5 NORTH GENESEE STREET  
WAUKEGAN, ILLINOIS

WILFRED E. HALL  
1926-1934

January 13, 1937

North Shore Coke and Chemical Company,  
A Delaware Corporation.

Gentlemen:

Our examination of the abstract and guaranty policy furnished to us by you of the title to the property hereinafter described is completed to include December 6, 1936, and on said date we find title of record as shown by said abstract and guaranty policy as follows:

NORTH SHORE COKE AND CHEMICAL COMPANY, a Delaware corporation,

subject to the following:

- (1) Rights or claims of parties in possession, unrecorded contracts of sale, and questions of survey.
- (2) Mechanic's lien claims, if any, where no notice thereof appears of record.
- (3) Special assessments and special taxes, if any, not confirmed by a court of record.
- (4) Taxes for the years 1936 and 1937.
- (5) Zoning and building ordinances.
- (6) Possible judgments, decrees or bankruptcy proceedings in the United States District Court affecting said premises.
- (7) Streets and highways.
- (8) Switch tracks, switch spurs and railroad rights of way.
- (9) Slips and waterways.
- (10) Rights of the Public and of the United States Government in and to so much of premises in question as are covered by the waters of Lake Michigan.
- (11) Rights of the Public and of the State of Illinois in and to so much of said premises as may have been formed by other than natural accretions.
- (12) Rights of the United States Government, State of Illinois, City of Waukegan, the Public and of the adjoining owners to have maintained in its present location the harbor and any piers contiguous thereto.

ALBERT L. HALL  
MINARD E. HULSE  
HARRY A. HALL  
MARSHALL MEYER

LAW OFFICES  
**HALL AND HULSE**  
5 NORTH GENESEE STREET  
WAUKEGAN, ILLINOIS

WILFRED E. HALL  
1926-1934

-2-

- (13) Rights of the Elgin, Joliet and Eastern Railroad Company, a corporation of Illinois, in and to all that portion of premises in question used and occupied by the tracks, spurs and switch tracks of said Railroad Company as reserved in the warranty deed from said Railroad Company, to William A. Baehr, dated March 14, 1927 and recorded on March 16, 1927, in Book 262 of Deeds, page 610 as Document 295717.
- (14) Agreement contained in the deed from the Elgin Joliet and Eastern Railroad Company, a corporation of Illinois, to William Baehr, dated March 14, 1927 and recorded on March 16, 1927 as document 295717, to maintain that part of the channel lying within premises in question as it now exists and that he will on demand of the Elgin, Joliet and Eastern Railroad Company extend said channel Northerly upon the Westerly side of premises in question, the same width as the present channel upon the Southerly portion of premises in question, providing that the owner of the land lying West thereof shall extend his portion of said channel and to keep and maintain said channels of a depth sufficient for all lake going vessels desiring to use said channel and to maintain a dock or retaining wall along the Easterly side of said channel and to keep the same clear from obstruction for the carrying on of traffic to Waukegan Harbor and other points. For further particulars see record.
- (15) Rights of the persons owning the premises South and adjoining premises in question and North of the Waukegan Harbor, to establish a roadway 50 feet wide across premises in question, parallel to the shores of Lake Michigan as it would then exist with the Westerly line thereof 100 feet from such shore line, with the right of changes and re-locate to connect with the roadway across the property lying North and South of premises in question, for the passage of persons, automobiles, trucks and teams.
- (16) Rights reserved by the Elgin, Joliet and Eastern Railroad Company (a corporation) to lay down, maintain and operate railroad tracks and switch tracks on land 25 feet in width running substantially parallel to the shore line of Lake Michigan as it would exist at the time of such laying down and with the Westerly line of a strip 125 feet West of the shore line of said Lake.

ALBERT L. HALL  
WINARD E. HULSE  
HARRY A. HALL  
MARSHALL MEYER

LAW OFFICES  
**HALL AND HULSE**  
5 NORTH GENESEE STREET  
WAUKEGAN, ILLINOIS

WILFRED E. HALL  
1926-1934

-3-

- (17) Perpetual easement contained in grant from North Shore Coke and Chemical Company to the City of Waukegan, dated July 31, 1935 and recorded August 2, 1935 as Document 415322 to maintain and use a roadway on and along the westerly 50 feet of the easterly 100 feet of said premises. For further particulars see record.
- (18) Agreement between North Shore Gas Company and North Shore Coke and Chemical Company, a corporation, dated February 17, 1927 and recorded April 8, 1927 as Document 296985 for the furnishing of a gas supply to the North Shore Gas Company by the North Shore Coke and Chemical Company. For further particulars see record.
- (19) Trust Indenture from North Shore Coke and Chemical Company, a corporation, to Central Trust Company of Illinois, dated March 7, 1927 and recorded April 3, 1927 in Book 408 of mortgages, page 56 as Document 296986, given to secure its bonds of even date therewith, payable to the order of bearer, due March 1, 1947, with interest at 6 per cent per annum, payable on the first of March and September in each year, evidenced by interest coupons of even date therewith, together with any further costs or charges accrued or to accrue under the terms of said trust indenture and the covenants, agreements and conditions therein contained, for full particulars of which you are hereby referred to the original instrument or the record thereof.  
(The Central Republic Trust Company, successor trustee to Central Trust Company of Illinois in said trust indenture, resigned as such trustee, and the City National Bank and Trust Company of Chicago was appointed successor trustee, by instrument recorded July 5, 1934 as Document 401752.)

This examination refers to property described as:

That part of the North West quarter of Section twenty-two (22), Township forty five (45) North, Range twelve (12), East of the Third Principal Meridian, described as follows: Commencing at the South West corner of the North West quarter of said Section twenty two (22); thence North Easterly, making a North East angle of eighty nine (89) degrees, twenty nine (29) minutes, with the East and West center line of said Section twenty-two (22) to a point on the North line of City Street, sixty six (66) feet from, (measured at right angles), the East and West center line of said Section twenty-two (22); thence East with and along the North line of said City Street, parallel to the East and West center line of said Section twenty-two (22), five hundred eighty



BERT L. HALL  
NARD E. HULSE  
ARRY A. HALL  
MARSHALL MEYER

LAW OFFICES  
**HALL AND HULSE**  
5 NORTH GENESEE STREET  
WAUKEGAN, ILLINOIS

WILFRED E. HALL  
1926-1934

-4-

five and thirty seven one hundredths (535.37) feet to a point on the North Westerly line of Harbor Street; thence North Easterly with and along said North Westerly line of Harbor Street and making a North Easterly angle of seventy five (75) degrees, twelve (12) minutes and ten (10) seconds with last described course extended East one hundred nineteen and forty three one hundredths (119.43) feet to a point; thence East parallel to and one hundred eighty one and forty seven one hundredths (181.47) feet from, (measured at right angles), the said center line of Section twenty two (22), three hundred seventy three and sixty one one hundredths (373.61) feet to a point; thence North Easterly making a North Easterly angle of sixty (60) degrees, one (1) minute and fifteen (15) seconds with last described course extended East four hundred seventeen and forty four one hundredths (417.44) feet for a place of beginning; thence East parallel to and five hundred forty three and six one hundredths (543.06) feet from, (measured at right angles), the said center line of said Section twenty two (22) and making a South Easterly angle of one hundred nineteen (119) degrees, fifty eight (58) minutes and forty five (45) seconds with last described course, thirteen hundred eighty nine and forty nine one hundredths (1389.49) feet more or less to a point on the shore line of Lake Michigan, (this course to be known as the first course); thence North Westerly with and along said shore line, to an intersection with a line running parallel with and fourteen hundred twenty (1420) feet North of (measured at right angles) the South line of the property herein described, (being the said first course), said shore line being described as follows, running Northerly and making a North Westerly angle of eighty eight (88) degrees, fifty five (55) minutes with said first course, one hundred seventy nine and sixteen one hundredths (179.16) feet to a point; thence North Easterly continuing along the shore of Lake Michigan and making a North Easterly angle of four (4) degrees, fifty nine (59) minutes and fifteen (15) seconds with last described course extended Northerly six hundred seventy five and five tenths (675.5) feet to a point; thence continuing North Easterly with and along said shore line and making a North Easterly angle of four (4) degrees, fifty two (52) minutes and forty five (45) seconds with last described course, extended Northerly five hundred seventy three and sixty seven one hundredths (573.67) feet to a point, (this course

ERT L. HALL  
AND E. HULSE  
IRY A. HALL  
SHALL MEYER

LAW OFFICES  
**HALL AND HULSE**  
5 NORTH GENESEE STREET  
WAUKEGAN, ILLINOIS

WILFRED E. HALL  
1926-1934

-5-

along said shore line to be known as second course); thence West twelve hundred fifty and thirty nine one hundredths (1250.39) feet to a point, (this course to be known as the third course), also being parallel to and fourteen hundred twenty (1420) feet North of (measured at right angles) the South line of property herein described; thence South Westerly making a South Easterly angle of one hundred (100) degrees, thirty one (31) minutes and thirty six (36) seconds with said third course, fourteen hundred thirty and two tenths (1430.2) feet to a point, (this course known as the fourth course); thence continuing South Westerly and making a South Westerly angle of nineteen (19) degrees, twenty seven (27) minutes and nine (9) seconds with last described course, extended Southerly sixteen and three one hundredths (16.03) feet to the place of beginning, in Lake County, Illinois.

Yours very truly,

HALL AND HULSE

By: 

MEH:E



# ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

P. O. BOX 380 JOLIET, ILLINOIS 60434

815-740-6622

September 19, 1989

Mr. Jon Currin  
North Shore Gas  
3001 Grand Avenue  
Waukegan, Illinois 60085

RECEIVED  
SEP 21 1989  
Engineering Dept

RE: Prior Entry Permit

Dear Mr. Currin:

Attached is an original and one copy of a Prior Entry Permit allowing your company permission to enter upon the property of the EJ&E Railway Company for the purpose of installing a 6" gas pipeline at Waukegan, Illinois. Please sign both copies and return to us. Upon execution, a copy will be returned for your file. As we previously discussed, a formal licence agreement will be executed, when presented. We will also need your contractor's Certificate of Insurance before this work begins.

We ask that you contact the Railway at least seventy-two hours in advance of your intent to enter our property by phoning D. R. Miselman, Administrative Supervisor, at 219-883-4711.

Very truly yours,

H. F. Nelson  
Director Engineering Services

HFN:k

Attachment

Prior Entry Permit

September 20, 1989

Mr. Jon Currin  
North Shore Gas  
3001 Grand Avenue  
Waukegan, Illinois 60085

Dear Sir:

Upon endorsement approving addressee's submission and acceptance of the terms and conditions of this letter, Elgin, Joliet and Eastern Railway Company ("Railway") hereby gives the addressee permission and authority to come upon the Railway's property for the installation of a 6" gas pipeline at or near Sta. No. -26.00 at Waukegan, Illinois, as shown on Exhibit "A" dated September 19, 1989.

Licensee agrees to execute a formal license agreement, covering the above installations and occupations, when presented.

In consideration of permission and authority to use the aforesaid property, addressee, by execution and submission of this letter to the Railway accepts all of the terms and conditions stated herein and covenants and agrees that:

Said permission and authority shall be exercised only in strict compliance with said terms and conditions and such other terms and conditions as the Railway, from time to time, may advise of in writing, the safety and continuity of operations of the Railway being recognized as of primary importance at all times;

Addressee shall reimburse the Railway for any and all loss or damage and shall indemnify, save harmless and defend the Railway from and against any and all suits, actions, legal proceedings, claims, demands, damages, costs, expenses and attorneys' fees in any manner caused by, arising from, incident to, connected with or growing out of this letter or the use of the property of the Railway for said Purpose;

Addressee covenants and agrees to release the Railway from all claims for loss or damage to equipment of addressee, or any part or parts thereof and from injury to or death of addressee or any person or persons upon property of the Railway in connection with said Purpose;

The Chief Engineer of the Railway shall be given not less than 72 hours' notice, in advance, of the time of entry upon property of the Railway;

Addressee shall furnish to said Chief Engineer, prior to the commencement of any entry upon property of the Railway, evidence of insurance coverage written by a company and in an amount which shall protect the Railway to its satisfaction from liability resulting from use of its property for said purposes;

When, in the opinion of said Chief Engineer, flagging or other methods shall be required to protect property of the Railway during the performance of any work connected with said Purpose, the cost thereof shall be paid promptly by the addressee upon receipt of bills therefor as shall all bills rendered for reimbursement to the Railway of the cost of work of any nature incurred in connection with said Purpose, including any cost which may be incurred to restore said property to a condition satisfactory to said Chief Engineer upon termination of said permission and authority and for any damage sustained by property of the Railway in connection with said Purpose and upon request the estimated amount of any such cost and expense shall be deposited with the Railway, in advance, with necessary adjustments to cover actual costs to be made when such shall be determined;

Said permission and authority does not include the right to move equipment or vehicles over any unprotected track of the Railway and any such movement shall be made at the nearest properly installed crossing or if no crossing exists reasonably close to the area of work, then upon payment of cost thereof by addressee, the Railway shall install a temporary crossing;

Said permission and authority shall terminate at the end of the work day October 31, 1989.

ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

The above terms and conditions are accepted and this letter submitted this 22nd day of September, 1989.

North Shore Gas Company  
(Name of Addressee)

BY: P. J. Doyle Vice President  
(Give corporate title and have attested by corporate officer if addressee is incorporated)

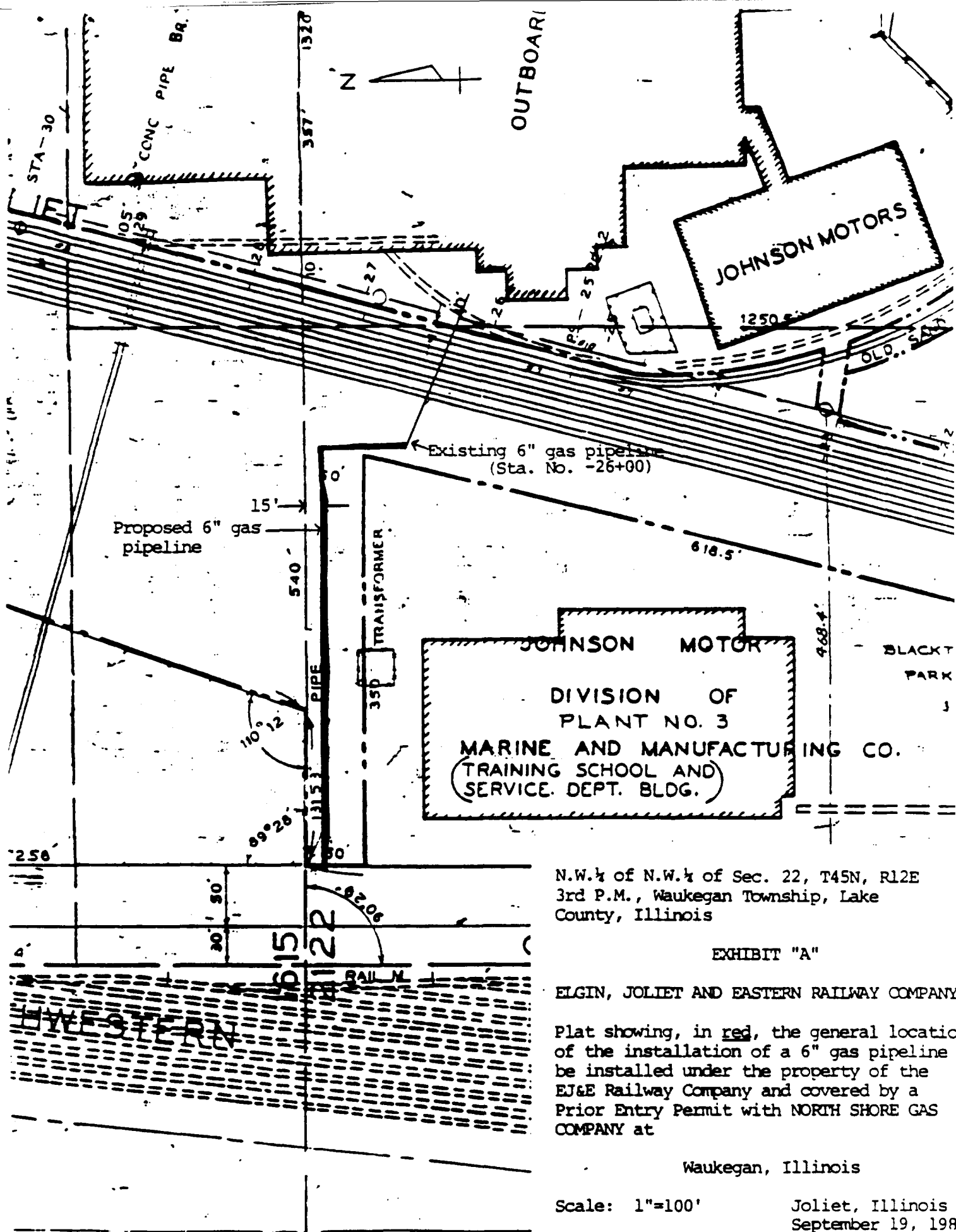
ATTEST:

[Signature] (Corporate Seal)  
Assistant Secretary

ON BEHALF of the  
Elgin, Joliet and  
Eastern Railway  
Company, the sub-  
mission is approved  
and permission and  
authority is given  
as above provided  
this \_\_\_\_\_ day of  
\_\_\_\_\_, 1989.

BY: \_\_\_\_\_

Title: Director Eng-  
ineering Services





# CERTIFICATE OF INSURANCE

## Wausau Insurance Companies

This is to certify that the insurance policies (described below by a policy number) written on forms in use by the company have been issued. This certificate is not a policy or a binder of insurance and does not in any way alter, amend or extend the coverage afforded by any policy referred to herein.

Name and Mailing Address of Insured

MUELLER PIPELINERS, INC.  
P.O. BOX 123  
NEW BERLIN, WI 53151

Producer No: 2696  
Office: MILWAUKEE, WI 53216  
Date: 9/21/89  
Region: XL

Type of Insurance	CO NO	Policy Number	Policy Effective Date (MO/DAY/YR)	Policy Expiration Date (MO/DAY/YR)	• • Unless otherwise indicated, this policy affords full coverage under Workers Compensation laws of all states (except states where coverage can be provided only by State Funds, and Canada) and as designated in the policy and endorsements for Part Two (Employers Liability).
Workers Compensation • •	2	0410 02 081464	04 01 89	04 01 90	Liability Limits in Thousands (\$00 omitted)
Commercial General Liability	3	0420 06 081464	04 01 89	04 01 90	General Aggregate \$ 1,000
Commercial Package or Trademark (Section II only)					Products & Comp/Ops. Aggregate \$ 1,000
( ) Claims Made (X) Occurrences					Personal Automobile Injury \$ 1,000
Products - Completed Operations: (X) Included ( ) Excluded					Each Occurrence \$ 1,000
Owners & Contractors Protective Liability	3	0420 04 093348*	04 01 89	04 01 90	Fire Damage (Any One Fire) \$ EXCLUDED
(X) All Owned Autos					Medical Expense (Any One Person) \$ EXCLUDED
( ) Specified Autos Only					Aggregate \$
(X) Hired Autos					Each Occurrence \$
(X) Nonowned Autos					Single Limit - Each Accident \$ 1,000
Umbrella Liability					Bodily Injury
					Each Person \$
					Each Accident \$
					Property Damage
					Each Accident \$
					Each Occurrence \$
					General Aggregate \$
					Retention \$

Special Provisions/Locations/Specified Autos: WISCONSIN & ELSEWHERE IN THE UNITED STATES

WRITTEN UNDER MUELLER RESOURCE MANAGEMENT, INC.

IF ANY POLICY DESCRIBED ABOVE IS CANCELED DURING ITS TERM BY THE COMPANY OR THE COVERAGE AFFORDED BY IT IS REDUCED, THE INSURER WILL MAIL NOTICE 30 DAYS BEFORE THE EFFECTIVE DATE OF SUCH CANCELATION OR CHANGE TO THE PARTY NAMED BELOW.

Notwithstanding any requirement, term or condition of any contract or other document with respect to which this certificate may be issued or may pertain, the insurance afforded by the policy (policies) described above is subject to all of the terms, exclusions and conditions of such policy (policies) during the term(s) thereof.

The entry of a number in this column means that the coverage is afforded by the company designated by the same number.

Issued to:

E. J. & E. Railroad  
Joliet, Illinois

\*Issuing Company No. 02. EMPLOYERS INSURANCE OF WAUSAU A Mutual Company  
03. WAUSAU UNDERWRITERS INSURANCE COMPANY  
07. ILLINOIS EMPLOYERS INSURANCE OF WAUSAU  
01. WAUSAU LLOYDS

Signed R. E. Schell



# CERTIFICATE OF INSURANCE

## Wausau Insurance Companies

This is to certify that the insurance policies (described below by a policy number) written on forms in use by the company have been  
is certificate is not a policy or a binder of insurance and does not in any way alter, amend or extend the coverage afforded by any policy re  
to herein.

Name and Mailing Address of Insured

MUELLER PIPELINERS, INC.  
P.O. BOX 325  
NEW BERLIN, WI 53151

Producer No.: 2696  
Office: MILWAUKEE, WI 53216  
Date: 9/21/89  
Region: ML

Type of Insurance	CO. NO.	Policy Number	Policy Effective Date (MO/DA/YR)	Policy Expiration Date (MO/DA/YR)	• • Unless otherwise indicated, this policy affords full coverage on Workers Compensation laws of all states (except states where co can be provided only by State Funds, and Canada) and as does in the policy and endorsements for Part Two (Employers Liability)
Workers Compensation • •	2	0410 02 081464	04 01 89	04 01 90	
Commercial General Liability	3	0420 06 081464	04 01 89	04 01 90	Liability Limits in Thousands (\$00 omitted)
Commercial Package or Trademark (Section II only)					General Aggregate \$ 1.00
( ) Claims Made (X) Occurrences					Products & Comp./Ops. Aggregate \$ 1.00
Products - Completed Operations: (X) Included ( ) Excluded					Personal & Advertising Injury \$ 1.00
Owners & Contractors Protective Liability					Each Occurrence \$ 1.00
					Fire Damage (Any One Fire) \$ EXCLUD
					Medical Expense (Any One Person) \$ EXCLUD
					Aggregate \$
					Each Occurrence \$
					Single Limit - Each Accident \$ 1.00
					Bodily Injury
					Each Person \$
					Each Accident \$
					Property Damage
					Each Accident \$
					Each Occurrence \$
					General Aggregate \$
					Retention \$

Special Provisions/Locations/Specified Areas: WISCONSIN & ELSEWHERE IN THE UNITED STATES

\*WRITTEN UNDER MUELLER RESOURCE MANAGEMENT, INC.

IF ANY POLICY DESCRIBED ABOVE IS CANCELED DURING ITS TERM BY THE COMPANY OR THE COVERAGE AFFORDED BY IT IS REDUCED, THE INSURER WILL MAIL NOTICE 30 DAYS BEFORE THE EFFECTIVE DATE OF SUCH CANCELATION OR CHANGE TO THE PARTY NAMED BELOW.

Notwithstanding any requirement, term or condition of any contract or other document with respect to which this certificate may be issued or may pertain, the insurance afforded by the policy (policies) described above is subject to all of the terms, exclusions and conditions of such policy (policies) during the term(s) thereof.

\* The entry of a number in this column means that the coverage is afforded by the company designated by the same number.

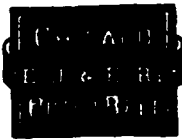
Issued to:

E. J. & E. Railroad  
Joliet, Illinois

\*Issuing Company No. 02. EMPLOYERS INSURANCE OF WAUSAU A Mutual Com  
03. WAUSAU UNDERWRITERS INSURANCE COMPANY  
07. ILLINOIS EMPLOYERS INSURANCE OF WAUSAU  
01. WAUSAU LLOYDS

Signed R. E. Schilling  
Authorized Representative





## ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

RECEIVED

DEC 5 1974

PLEASE REMIT TO:

Engineering Dept. P. O. BOX 92363  
CHICAGO, ILLINOIS 60690North Shore Gas Company  
209 Madison Street  
Waukegan, Illinois 60085TO INSURE PROPER CREDIT  
WHEN REMITTING REFER TO:BILL NO. 124029DATE: December 1, 1974

PAYMENT DUE 30 DAYS AFTER RECEIPT OF BILL, UNLESS OTHERWISE PROVIDED FOR BY CONTRACT.

For permission and authority to install, maintain and operate a 6-inch gas main in a 10-inch casing, across and underneath the surface of our right-of-way and tracks near Station 26 + 070 at Waukegan, Illinois from December 15, 1974 to December 14, 1975, inclusive, as per contract dated December 15, 1948.

Rental Per Annum

\$12.00

## DISTRIBUTION

140 - 510 - 459 \$12.00

ADDRESS ALL COMMUNICATIONS  
RELATIVE TO THIS BILL TOMANAGER - DISBURSEMENTS  
& GENERAL ACCOUNTING  
EJ&E RY. CO., P.O. BOX 880  
JOLIET, ILLINOIS 60434

LICENSE ENDORSEMENT

It is mutually understood and agreed by the parties hereto that effective the **1st** day of **April**, 1978 the license agreement made and entered into the **15th** day of **December**, 1948 be and same is supplemented and amended hereby as follows:

On and after the effective date hereof, the annual payment to be made as provided in said agreement shall be and become the sum of **\$110.00** in place of the amount as stated therein.

Except to the extent hereinabove provided in this License Endorsement all of the terms, conditions, covenants, stipulations and provisions of said license agreement above identified shall continue in full force and effect as therein stated.

IN WITNESS WHEREOF, the parties hereto have executed these presents in duplicate originals, the **25TH** day of **APRIL**, 1978, effective as of the day and the date first above written.

ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

By:

J E Arado  
Director of Industrial Development  
and Real Estate

NORTH SHORE GAS COMPANY

By:

Louis A. Baldraf  
Jan 11/13

ATTEST:

D. O. Hoem  
ASSISTANT SECRETARY

AGREEMENT

between

ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

and

NORTH SHORE GAS COMPANY

Dated: December 15, 1948.

THIS AGREEMENT, made and entered into this 15th day of December, 1948, by and between the ELGIN, JOLIET AND EASTERN RAILWAY COMPANY, a corporation (hereinafter termed the "Railway"), party of the first part, and NORTH SHORE GAS COMPANY, a corporation (hereinafter termed the "Gas Company"), party of the second part:

W I T N E S S E T H:

FIRST: The Railway hereby grants to the Gas Company permission and authority to install, maintain and operate a six (6) inch gas main, together with a casing having a diameter of not less than ten (10) inches, across and underneath the surface of the right of way and tracks of the Railway in the Southwest Quarter (SW 1/4) of the Southwest Quarter (SW 1/4) of Section Fifteen (15), and in the Northwest Quarter (NW 1/4) of the Northwest Quarter (NW 1/4) of Section Twenty-two (22), Township Forty-five (45) North, Range Twelve (12) East of the Third Principal Meridian in Lake County, Illinois. The location of said gas main is shown in red on the plat attached hereto, marked Exhibit "A" and made a part hereof.

SECOND: The Gas Company agrees to pay to the Railway, at the office of the Railway in the City of Chicago, Illinois the following:

- (1) The sum of Twenty-five Dollars (\$25.00) immediately upon the execution of this agreement.
- (2) The further sum of Twelve Dollars (\$12.00) on the date of this agreement and the sum of Twelve Dollars (\$12.00) upon the corresponding date of each year after the date of this agreement.

THIRD: The Gas Company agrees that where said gas main crosses underneath the tracks of the Railway it shall be installed inside a casing having a diameter of not less than ten (10) inches, and that the top of said casing shall be not less than four and five tenths (4.5) feet below the base of the lowest rail in the tracks, and that neither end of said casing shall be less than forty-five (45) feet from the center line of the track nearest thereto, measured at right angles thereto. Each end of said casing shall be sealed and a vent pipe of not less than two (2) inches in diameter shall be installed at each end thereof, which vent pipes shall be fastened to the top of the casing at the high end and to the side or bottom of the casing at the low end. The top of each of said vent pipes shall be fitted with a down turned elbow properly screened at a height of not less than four (4) feet above the surface of the ground. Said gas main, casing and vent pipes shall be installed and maintained in accordance with the "Specifications for Pipe Line Crossings under Railway Tracks," adopted in 1933 by the American Railway Engineering Association, as amended.

FOURTH: The Gas Company agrees to install, maintain and operate said gas main, casing and vent pipes (hereinafter for convenience collectively termed "equipment") at all times in accordance with all laws and ordinances that may be applicable thereto, and also in accordance with the rules and regulations of the proper public authorities now or at any time hereafter having jurisdiction thereof. The Gas Company also agrees to reimburse the Railway for all expense which the Railway may be put to or incur at any time or from time to time by reason of the installation, maintenance, operation, repair or removal of said equipment, and each and every part thereof.

FIFTH: It is understood and agreed that said equipment shall be maintained, operated and kept in good order and repair by the Gas Company at all times, and at the Gas Company's expense, in a manner satisfactory to the Chief Engineer of the Railway. The quality and character of said equipment shall be satisfactory to, and the exact locations thereof, shall be subject to the approval of said Chief Engineer.

SIXTH: In case the Railway at any time shall desire any repairs to or replacements of said equipment, or any part thereof, then the Gas Company shall make such repairs or replacements, as the case may be, within ten (10) days after written notice shall have been sent or given by the Railway to the Gas Company so to

do. In case the Gas Company shall fail to make such repairs or replacements within ten (10) days after such notice is sent or given as aforesaid, then the Railway may make such repairs or replacements and the Gas Company shall pay to the Railway immediately thereafter the entire cost and expense thereof.

SEVENTH: It is understood and agreed that the Gas Company may enter upon the property of the Railway at all reasonable times for the purpose of maintaining, repairing or renewing said equipment. It is understood, however, that all such work of maintenance, repair and renewal shall be done in a proper manner and without injury to said property of the Railway, and the Gas Company shall remove all materials and rubbish and shall fill up and tamp thoroughly all excavations made for the installation, maintenance, repair or renewal of said equipment, and shall keep the material covering said gas main at the same level as the ground adjacent thereto at all times during the life of this agreement.

EIGHTH: The Gas Company covenants and agrees to release the Railway from all claims for loss or damage to said equipment, or any part or parts thereof, however caused or occasioned, whether by the negligence of the employees of the Railway, or otherwise.

NINTH: The Gas Company covenants and agrees to indemnify, save harmless and defend the Railway from and against all suits, actions, legal proceedings, claims, demands, damages, costs, expenses and attorneys' fees in any manner caused by, arising from, incident to, connected with or growing out of the installation, maintenance, operation, repair, renewal, alteration in location, use, existence, leakage or removal of said equipment or any part or parts thereof.

TENTH: The Gas Company shall pay before delinquency all general and special taxes and special assessments that may be levied, charged or assessed upon said equipment. In the event, however, that said equipment shall be considered or assessed as a part of the property of the Railway, the Gas Company shall pay to the Railway the amount which the Railway has been obligated to pay due to the presence of said equipment upon said property of the Railway. If the Gas Company shall fail to pay such taxes and assessments when due, the Railway shall have the right but shall not be obligated to pay such taxes or assessments. The amount so paid by the Railway shall be repaid to the Railway by the Gas Company immediately.

ELEVENTH: This agreement and the permission and authority herein given may be terminated at any time by either party hereto by sending or giving to the other party notice in writing that on



a certain date this agreement and said permission and authority immediately shall cease and terminate. Said written notice shall be sent or given not less than thirty (30) days prior to the date of termination specified in said notice. The Gas Company, upon the termination of said permission and authority in the manner aforesaid, or in any other manner, if requested so to do by the Railway, immediately shall remove said equipment and each and every part thereof from the property of the Railway, and shall restore said property to a condition equal to that which existed at the time of the installation of said equipment at the sole cost and expense of the Gas Company, and said Gas Company shall save the Railway harmless from any damage, injury or expense caused or occasioned by or incident to such removal unless the same be attributable to the negligent act or omission of the Railway. If the Gas Company shall fail to remove said equipment, as aforesaid, the Railway shall have the right to remove all or any portion of said equipment and to restore said premises as above mentioned, and the title to all of said equipment shall vest in the Railway and may be used or disposed of by the Railway in any manner which the Railway may desire. All of the costs and expenses incurred by the Railway in and by the performance of the work aforesaid shall be paid by the Gas Company to the Railway. The termination of said permission and authority in any way shall not release the Gas Company from any liability to the Railway

which has accrued or which may accrue thereafter by reason of the violation by the Gas Company of any of the covenants or agreements herein contained.

TWELFTH: It is understood and agreed that any notice or demand in this agreement provided shall be deemed to have been given or made properly if and when placed in the United States mail, registered and addressed to the party to be notified at its last known principal office or place of business in the State of Illinois.

THIRTEENTH: It is understood and agreed that any failure by the Railway at any time, or from time to time, to enforce or require the strict keeping and performance by the Gas Company of any of the terms or conditions of this agreement shall not constitute a waiver by the Railway of such terms or conditions, and shall not affect or impair such terms or conditions in any way, or the right of the Railway at any time to avail itself of such remedies as it may have for any breach or breaches of such terms or conditions.

FOURTEENTH: It is covenanted and agreed by and between the parties hereto that this agreement shall inure to the benefit of and shall be and remain binding upon their respective successors and assigns.

IN WITNESS WHEREOF, the parties hereto have duly executed these presents in duplicate originals, the day and year first above written.



*[Handwritten signature]*

ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

By *W. E. Deaton*  
Industrial and Tax Commissioner

NORTH SHORE GAS COMPANY

By *Chas. L. ...*  
President

ATTEST:

*J. M. ...*  
Secretary

WAJ:lg  
12/7/48  
9875  
1-7





## ELGIN, JOLIET & EASTERN RAILWAY COMPANY

Real Estate Department  
P.O. Box 880  
Joliet, Illinois 60434

**RECEIVED**

FILE: 111480006

MAR 1 1988

February 26, 1988

Engineering Dept.

Mr. Russell W. Stegman  
Supervisory Engineer  
North Shore Gas Company  
3301 Grand Ave.  
Waukegan, IL 60085

Dear Mr. Stegman:

Attached for your records is a fully executed Endorsement to your License dated December 15, 1948 covering your use of Railway property at Waukegan, Illinois.

Sincerely,

R. A. Mays  
Real Estate Agent

Attachment

H. F. Nelson  
cc: ~~Chief Engineer~~  
Assistant Treasurer-  
Comptroller-

Copy of Endorsement attached  
Original Endorsement ~~and Check~~ attached.  
Your file: 8-490-90-6.  
Copy of Endorsement attached.

RE FORM 88

LICENSE ENDORSEMENT

#111480006

It is mutually understood and agreed by the parties hereto that effective the 1st day of April, 19 88 the certain License Agreement made and entered into the 15th day of December, 19 48 by the same is supplemented and amended hereby as follows:

On the effective date of this Endorsement and upon the corresponding date of each year thereafter the Licensee agrees to pay Licensor the sum of \$ 150.00, payable annually in advance, and that notwithstanding any other provisions of said License Agreement, it is understood and agreed that the Licensor from time to time as it may deem appropriate, but not earlier than the fifth anniversary of the effective date of the License Agreement and thereafter at intervals which shall not be more frequent than each fifth year, may increase or decrease the annual payment specified in this Endorsement and also may otherwise revise the License Agreement in whole or in part, as in the sole judgement of the Railway may be necessary. The Licensor agrees that it shall send or give to the Licensee not less than ninety (90) days written notice in advance of any such change or revision and shall specify the effective date thereof.

Except to the extent hereinabove provided in this License Endorsement all of the terms, conditions, covenants, stipulations and provisions of said License Agreement above identified shall continue in full force and effect as therein stated.

IN WITNESS WHEREOF, the parties hereto have executed these presents in duplicate originals, the 10th day of February, 19 88, effective as of the day and the date first above written.

ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

By: H. C. Steins  
General Manager

LESSEE: NORTH SHORE GAS COMPANY

By: Henry A. Wagener  
Title: Engineer

R-102

LICENSE ENDORSEMENT

111480006

It is mutually understood and agreed by the parties hereto that effective the 1st day of April, 1983 the certain license agreement made and entered into the 15th day of December, 1948 be and same is supplemented and amended hereby as follows:

On the effective date of this Endorsement and upon the corresponding date of each year thereafter the Licensee agrees to pay Licensor the sum of \$ 150.00, payable annually in advance.

Except to the extent hereinabove provided in this License Endorsement all of the terms, conditions, covenants, stipulations and provisions of said license agreement above identified shall continue in full force and effect as therein stated.

IN WITNESS WHEREOF, the parties hereto have executed these presents in duplicate originals, the 4th day of April, 1983, effective as of the day and the date first above written.

ELGIN, JOLIET AND EASTERN RAILWAY COMPANY


By:



General Manager

NORTH SHORE GAS CO.

By:



Title:

Manager of Operations

## PAYMENT REQUEST

PAYEE Elgin, Joliet & Eastern Railway CompanyMAILING ADDRESS Manager - Disbursements and  
OR DEPARTMENT General AccountingCITY, STATE P. O. Box 880, Joliet, Ill. 60434  
ZIP CODEFORWARD E. J. & E. Railway  
CHECK TOREQUESTED BY B. H. Denenberg

PREPARATION DATE

2/3/72

VENDOR NUMBER

DUE DATE

ORDER NUMBER

TOTAL AMOUNT

\$51.00DO NOT  
PREPARE 1 ☐  
CHECKSPECIAL  
HANDLING 2 ☐  
REQUIREDINCLUDE IN PREVIOUS MONTH'S ESTIMATE OF ACCOUNTS PAYABLE ☐

FO	TRANS. CODE	AREA	FUNC- TION	W.O./JOB		COST CODE	TRANS TYPE	ITEM AMOUNT
				CODE	NUMBER			
8	480	171	1901				0	\$51.00
8							0	
8							0	
8							0	
8							0	
8							0	
8							0	
8							0	

FILE COPY 6

## DETAILED STATEMENT

To install, maintain and operate a 6" gas main in a 10" casing across and underneath the Elgin, Joliet and Eastern Railway Company property and track east of Sand Street, at Waukegan, Illinois.





Cash on hand

3/1/1955

W. J. & Co.

W. J. & Co.

\$ 51.00

W. J. & Co.

" "

Are we still paying

No. 2 2/531/57 MAR 4 1957 244423

(with 100 and 100)

851.00

ELGIN. JOLIET AND EASTERN RAILWAY COMPANY

208 SOUTH LASALLE STREET RRK:VMc

CHICAGO 4. ILL., March 6, 1950

WILLIAM E. DEATON  
INDUSTRIAL AND TAX COMMISSIONER  
RICHARD R. KNIGHT  
LAND AND TAX AGENT

*Mr. Mucholland -  
For the Document File*

*W.E.D.*

Mr. Wm. J. Muestenfeld  
Vice President-Charge of Operation  
North Shore Gas Company  
Waukegan, Illinois

Dear Sir:

Attached is fully executed copy of agreement dated  
February 1, 1950 with your company for a six inch gas main  
on our property at Waukegan, Illinois.

This for your files.

Yours truly,

*W.E. Deaton*  
Industrial and Tax Commissioner

Attach

described permits, licenses, agreements and/or easements were transferred and assigned by NORTH SHORE GAS COMPANY to LAKE GAS COMPANY (now known as NORTH SHORE GAS COMPANY):

<u>E.J.&amp;E. Ry. Co. File Number</u>	<u>Description</u>	<u>Date of Instrument</u>
8-490-18-3	Gas main across right of way, North Chicago	4/01/49
8-490-18-4	Pipe crossing 22nd St., North Chicago	9/15/61
8-490-76-2	C.I. gas pipe under right of way, Rondout	9/14/17
8-490-76-4	16" gas main, Rondout	11/15/61
8-490-76-5	4" gas pipe, Bradley Rd., Rondout	10/01/63
8-490-88-2	Gas pipeline, Upton	12/09/32
8-490-90-2	Gas main, Waukegan	2/18/18
✓ 8-490-90-6	6" gas main, Waukegan	12/15/48
8-490-90-7	Gas main, Waukegan	2/01/50
8-645-18-29	Easement covering 3,384 sq. ft. of E.J.&E. property in North Chicago	5/01/59
8-1125-90-2	Gas main, Waukegan	12/01/13
8-1125-90-3	Gas main, Waukegan	2/04/13
8-1400-90-1	Gas pipe, Waukegan	12/03/13

day of February, 1961

NORTH SHORE GAS COMPANY



**ELGIN, JOLIET AND EASTERN RAILWAY COMPANY**

P O BOX 880 JOLIET ILLINOIS 60434

815 / 740-6622

September 27, 1989

Mr. Jon Currin  
North Shore Gas  
3001 Grand Avenue  
Waukegan, Illinois 60085

SUBJECT: Prior Entry Permit With North Shore Gas at  
Waukegan, Illinois

Dear Mr. Currin:

Attached is an original, executed Prior Entry Permit regarding the  
above-mentioned subject for your file.

Very truly yours,

H. F. Nelson  
Director Engineering Services

HFN:k

cc: D. K. Toftoy  
D. R. Miselman  
J. M. Restaino - original

Attachment

Prior Entry Permit

September 20, 1989

Mr. Jon Currin  
North Shore Gas  
3001 Grand Avenue  
Waukegan, Illinois 60085

Dear Sir:

Upon endorsement approving addressee's submission and acceptance of the terms and conditions of this letter, Elgin, Joliet and Eastern Railway Company ("Railway") hereby gives the addressee permission and authority to come upon the Railway's property for the installation of a 6" gas pipeline at or near Sta. No. -26.00 at Waukegan, Illinois, as shown on Exhibit "A" dated September 19, 1989.

Licensee agrees to execute a formal license agreement, covering the above installations and occupations, when presented.

In consideration of permission and authority to use the aforesaid property, addressee, by execution and submission of this letter to the Railway accepts all of the terms and conditions stated herein and covenants and agrees that:

Said permission and authority shall be exercised only in strict compliance with said terms and conditions and such other terms and conditions as the Railway, from time to time, may advise of in writing, the safety and continuity of operations of the Railway being recognized as of primary importance at all times;

Addressee shall reimburse the Railway for any and all loss or damage and shall indemnify, save harmless and defend the Railway from and against any and all suits, actions, legal proceedings, claims, demands, damages, costs, expenses and attorneys' fees in any manner caused by, arising from, incident to, connected with or growing out of this letter or the use of the property of the Railway for said Purpose;

Addressee covenants and agrees to release the Railway from all claims for loss or damage to equipment of addressee, or any part or parts thereof and from injury to or death of addressee or any person or persons upon property of the Railway in connection with said Purpose;

The Chief Engineer of the Railway shall be given not less than 72 hours' notice, in advance, of the time of entry upon property of the Railway;

Addressee shall furnish to said Chief Engineer, prior to the commencement of any entry upon property of the Railway, evidence of insurance coverage written by a company and in an amount which shall protect the Railway to its satisfaction from liability resulting from use of its property for said purposes;

When, in the opinion of said Chief Engineer, flagging or other methods shall be required to protect property of the Railway during the performance of any work connected with said Purpose, the cost thereof shall be paid promptly by the addressee upon receipt of bills therefor as shall all bills rendered for reimbursement to the Railway of the cost of work of any nature incurred in connection with said Purpose, including any cost which may be incurred to restore said property to a condition satisfactory to said Chief Engineer upon termination of said permission and authority and for any damage sustained by property of the Railway in connection with said Purpose and upon request the estimated amount of any such cost and expense shall be deposited with the Railway, in advance, with necessary adjustments to cover actual costs to be made when such shall be determined;

Said permission and authority does not include the right to move equipment or vehicles over any unprotected track of the Railway and any such movement shall be made at the nearest properly installed crossing or if no crossing exists reasonably close to the area of work, then upon payment of cost thereof by addressee, the Railway shall install a temporary crossing;

Said permission and authority shall terminate at the end of the work day October 31, 1989.

ELGIN, JOLIET AND EASTERN RAILWAY COMPANY

The above terms and conditions are accepted and this letter submitted this 22nd day of September, 1989.

North Shore Gas Company  
(Name of Addressee)

BY: [Signature] Vice President  
(Give corporate title and have attested by corporate officer if addressee is incorporated)

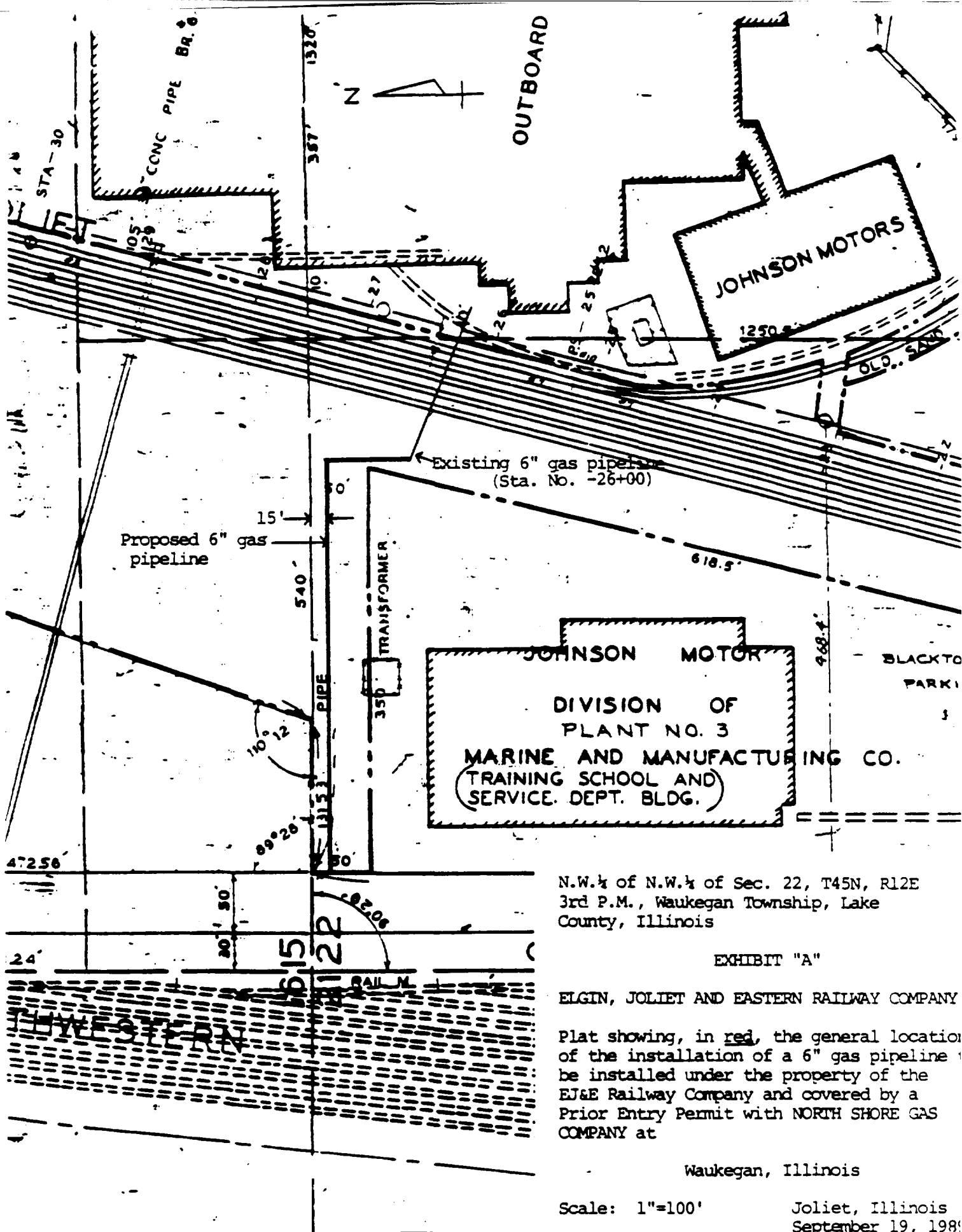
ATTEST:

[Signature] (Corporate Seal)  
Assistant Secretary

ON BEHALF of the  
Elgin, Joliet and  
Eastern Railway  
Company, the sub-  
mission is approved  
and permission and  
authority is given  
as above provided  
this 26<sup>th</sup> day of  
Sept., 1989.

BY: [Signature]

Title: Director Eng-  
ineering Services



**COPY**

September 25, 1989

Elgin Joliet and Eastern Railway Company  
P.O. Box 880  
Joliet, Illinois 60434  
Attn: Mr. H. F. Nelson  
Director Engineering Services

Re: E J & E Railroad Easement  
File No.: 111480006

Dear Sir:

Please find enclosed two executed prior entry permits and one certificate of insurance issued to the E J & E Railroad as you requested.

If you have any questions or require any additional information please contact me at (312) 336-7400 extension 313.

Very truly yours,

Jonathan M. Currin  
Senior Engineer

JMC:p  
encl.



DAHRINGER

ROAD

TO SAND ST.

RAILROAD

ELGIN, JOLIET & EASTERN

12" HD GAS

NORTH SHORE SANITARY DISTRICT

NORTH SHORE GAS CO.		WAUKEGAN, ILLINOIS	
SEE OTHER		EXHIBIT 'A'	
DATE SW. 8-18-74	DATE SW. 8-18-74	BY SW. 8-18-74	
DATE BY 04/18/80	DATE BY 04/18/80	DATE BY 04/18/80	
SCALE 1/4" = 10'	SCALE 1/4" = 10'	SCALE 1/4" = 10'	

WAUKEGAN TOWNSHIP  
S.W. 1/4 SECTION 15  
N.W. 1/4 SECTION 22  
T 45 N - R 12 E - 3 PM.

12" HD GAS MAIN

PARKING LOT

E.T.E. RR. RIGHT-OF-WAY

JOHNSON MOTORS  
DIVISION OF OUTBOARD MARINE CORPORATION

LAKE MICHIGAN

PAVEMENT

SEA HORSE DRIVE

REGULATOR VAULTS

1677453

## AGREEMENT

THIS AGREEMENT, made and entered into this 26<sup>th</sup> day of JUNE, A.D. 1974, by and between OUTBOARD MARINE CORPORATION, a Delaware Corporation with its corporate office at 100 Sea Horse Drive, Waukegan, Illinois 60085, hereinafter referred to as "CORPORATION", and NORTH SHORE GAS COMPANY, an Illinois Corporation, 3001 Grand Avenue, Waukegan, Illinois 60085, hereinafter referred to as "LICENSEE".

**WITNESSETH:**

The CORPORATION for and in consideration of the terms, covenants, agreements and conditions hereinafter contained on the part of the LICENSEE to be made, performed, kept and observed by these presents, does give and grant unto LICENSEE, but without warranty, subject to the exceptions, reservations, conditions, limitations and provisions hereinafter set forth, the right and privilege to install, operate, maintain, repair, replace and remove a 12-inch gas main, hereinafter referred to as facility, in, under and across CORPORATIONS property located in the South half of Section 15 and the North half of Section 22, Township 45 North, Range 12, East of the Third Principal Meridian, Mankato, Lake County, Illinois, said facility is to be along the centerline as shown on the drawing marked "EXHIBIT A", attached hereto and hereby made a part hereof.

The rights and privileges herein granted by CORPORATION are accepted by  
LICENSEE upon the following terms, covenants and conditions:

FIRST: LICENSEE shall notify CORPORATION's office at least forty-eight (48) hours in advance, except in case of emergency repairs and in cases of routine inspection and operation, before entering upon said property of CORPORATION to make the herein proposed installation, replacement or removal thereof, in order that the CORPORATION can locate its underground facilities (if any) and have a representative or representatives present at such time or times if it so desires and LICENSEE agrees that all work in said property shall be done to the satisfaction of said representative or representatives of said CORPORATION.

SECOND: LICENSEE agrees that said facility will be installed in CORPORATION property in strict conformity with said "EXHIBIT A" attached hereto. Any proposed changes in said plans, before or after installation, shall be submitted to CORPORATION for its written approval and no work shall be commenced until such

1677453

**Prepared By:**  
**A. J. H. HARRIS, Attorney**  
**122 S. W. 7th Avenue**  
**Coral Gables, Florida 33134**

written approval has been obtained.

THIRD: The rights herein are given subject to any use now made of said property by CORPORATION, its grantees, licensees and lessees, and should CORPORATION desire to make any use of said premises hereafter with which said facility will in any manner interfere, LICENSEE agrees that it will, at its sole cost and expense, within one hundred and twenty (120) days after receiving written notice from CORPORATION, make such changes in said facility as, in the judgment of CORPORATION, may be required to avoid interference with the use or proposed use of its property. LICENSEE agrees to relocate said facility to another location designated by CORPORATION in said property acceptable to LICENSEE.

FOURTH: LICENSEE shall indemnify, save and hold harmless the CORPORATION, its employees, agents and assigns free and harmless from any and all damages, costs and liabilities, including defense of lawsuits and claims which may in any way result from any occurrence as a result of the activity of the LICENSEE, its employees, agents or assigns.

FIFTH: LICENSEE agrees to restore the surface of said CORPORATIONS property, in connection with said facility, damaged by the construction, installation, operation, maintenance, repair, renewal or removal of such facility or related facilities, to the condition of said property immediately before such damage occurred and LICENSEE shall also be obligated to replace trees, shrubs or fences that are damaged or destroyed by the construction, installation, operation, maintenance, repair, renewal or removal of said facility and related facilities.

SIXTH: LICENSEE agrees that there shall be no impairment of natural or installed drainage facilities occasioned by the installation, repair, maintenance or removal of said facility.

SEVENTH: Termination of this agreement shall be to the satisfaction of both the CORPORATION and the LICENSEE.

EIGHTH: The terms "CORPORATION" and "LICENSEE" wherever used in this instrument are intended in each instance to include the respective successors and assigns of CORPORATION or LICENSEE, whichever the case may be, and all of the terms and provisions of this instrument shall inure to the benefit of and be binding upon the respective successors and assigns of CORPORATION and LICENSEE.

IN WITNESS WHEREOF, the parties hereto have caused this instrument to be executed in their respective names by their respective officers or representatives all as of the day and year first above written.

OUTBOARD MARINE CORPORATION

BY Carl P. Reed  
Vice President

ATTEST:

John H. Young  
Assistant Secretary

NORTH SHORE GAS COMPANY

BY W. B. Caldwell  
Vice President

ATTEST:

John H. Young  
Assistant Secretary

Approved & attested:  
1955

DOC 1677453

RECEIVED  
OFFICE OF THE SECRETARY OF THE TREASURY  
WASHINGTON, D.C.

NOV 27 74 AM 10 10

David J. H. H. H.  
Vice President

1677453  
North Shore Gas Co.  
207 Grand Ave.  
Beverly, Mass.  
1677453

# NORTH SHORE *Gas* COMPANY

3001 GRAND AVENUE - WAUKEGAN, ILLINOIS 60085  
TELEPHONE 336-9300

June 6, 1974

Mr. J. R. Seeger  
Secretary and Corporate Attorney  
Outboard Marine Corporation  
100 Sea Horse Drive  
Waukegan, Illinois 60085

Dear Mr. Seeger:

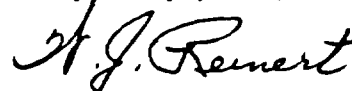
Attached is a draft of a proposed license agreement between North Shore Gas Company and the Outboard Marine Corporation.

Would you kindly review and advise me if this is an acceptable license agreement.

If so, I will make the necessary arrangements to have it executed by our Company and then forwarded to you for execution by Outboard Marine Corporation.

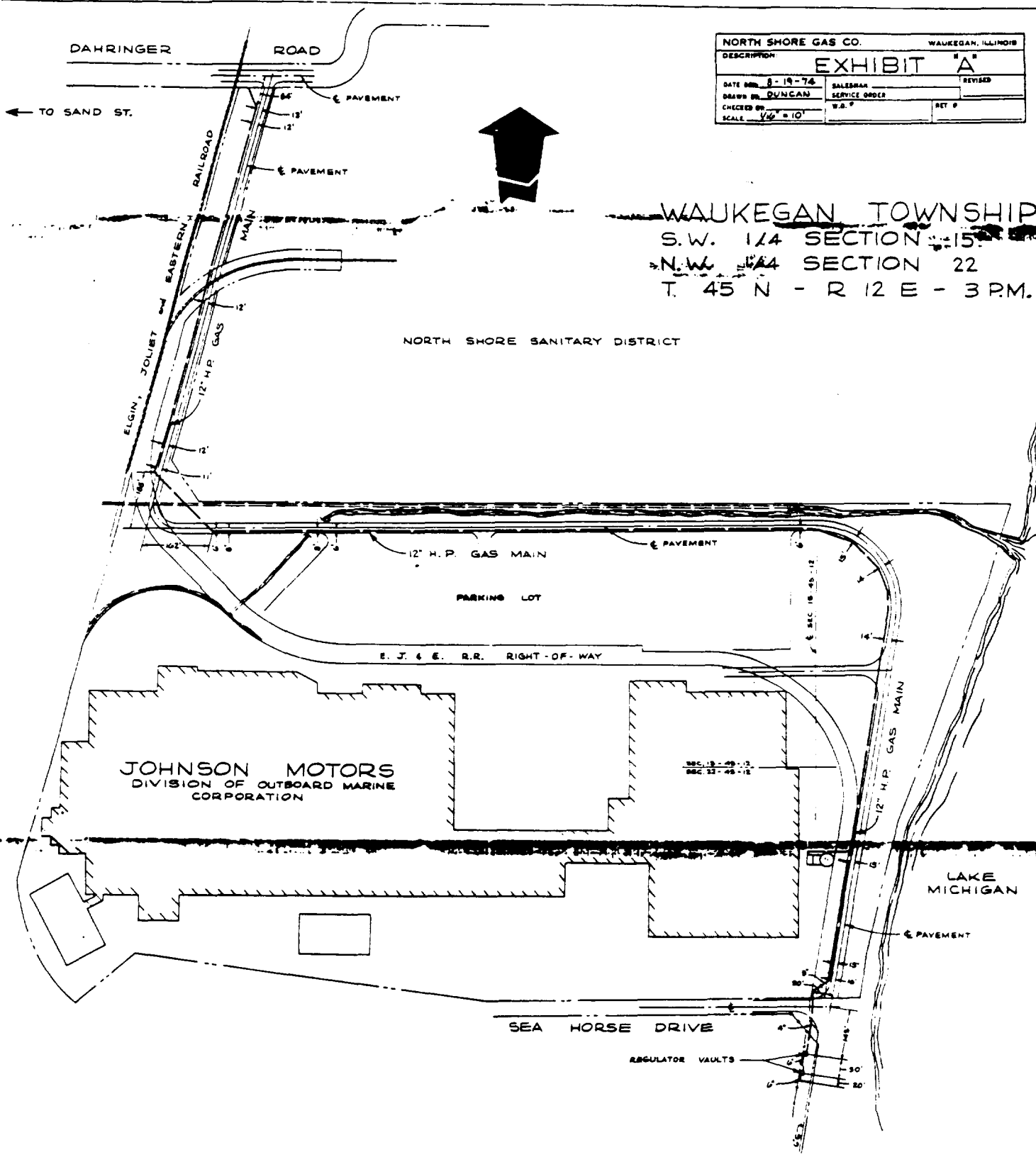
Please contact the undersigned at 336-9300 if you have any questions regarding this matter.

Very truly yours,



W. J. Reinert  
Supervisory Engineer

WJR:j  
Encl.



NORTH SHORE GAS CO.		WAUKEGAN, ILLINOIS	
DESCRIPTION		EXHIBIT "A"	
DATE DES. 8-19-74	SALESMAN	REVISED	
DRAWN BY DUNCAN	SERVICE ORDER		
CHECKED BY	W.S.P.	RET. #	
SCALE 1/4" = 10'			

WAUKEGAN TOWNSHIP  
S.W. 1/4 SECTION 15  
N.W. 1/4 SECTION 22  
T. 45 N - R 12 E - 3 P.M.

NORTH SHORE SANITARY DISTRICT

JOHNSON MOTORS  
DIVISION OF OUTBOARD MARINE  
CORPORATION

LAKE MICHIGAN

SEA HORSE DRIVE

REGULATOR VAULTS

# NORTH SHORE *Gas* COMPANY

3001 GRAND AVENUE - WAUKEGAN, ILLINOIS 60085  
TELEPHONE 334-9300

August 23, 1974

Mr. Robert M. Atkin  
Manager, Plant Engineering  
Johnson Outboards  
200 Sea Horse Drive  
Waukegan, Illinois 60085

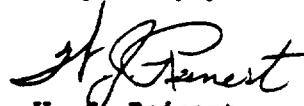
Dear Mr. Atkin:

I am enclosing for your records a fully executed and documented copy of a license agreement between our Companies.

Please place this agreement in proper file.

We appreciate your cooperation you have given us in this matter.

Very truly yours,



W. J. Reinert  
Supervisory Engineer

SJD/WJR:j  
Encl.

# NORTH SHORE *Gas* COMPANY

3001 GRAND AVENUE - WAUKEGAN, ILLINOIS 60085  
TELEPHONE 336-9300

June 6, 1974

Mr. J. R. Seeger  
Secretary and Corporate Attorney  
Outboard Marine Corporation  
100 Sea Horse Drive  
Waukegan, Illinois 60085

Dear Mr. Seeger:

Attached is a draft of a proposed license agreement between North Shore Gas Company and the Outboard Marine Corporation.

Would you kindly review and advise me if this is an acceptable license agreement.

If so, I will make the necessary arrangements to have it executed by our Company and then forwarded to you for execution by Outboard Marine Corporation.

Please contact the undersigned at 336-9300 if you have any questions regarding this matter.

Very truly yours,



W. J. Reinert  
Supervisory Engineer

WJR:j  
Encl.



# NORTH SHORE *Gas* COMPANY

3001 GRAND AVENUE - WAUKEGAN, ILLINOIS 60085  
TELEPHONE 336-9300

June 7, 1974

The Edward Gray Corp.  
12233 Avenue "O"  
Chicago, Illinois 60633

Attention: Mr. Gerald E. Guarnaccio

Re: Outboard Marine Corp.  
Gas Meter Building

Dear Sir:

Attached is a sketch showing a concrete regulator pad with foundation that North Shore Gas Company is proposing to be constructed adjacent to the north wall of the meter house you are building in conjunction with the Outboard Marine Corp. construction, Waukegan, Illinois.

Since you have men and equipment on the site we would be interested in your furnishing a proposal for this work.

Therefore, would you kindly submit an estimate for the necessary labor and material to construct the concrete meter pad as shown on the attached sketch.

Please contact the undersigned at 336-9300 if you have any questions regarding this matter.

Very truly yours,



W. J. Reinert  
Supervisory Engineer

WJR:j  
Encl.

AGREEMENT

THIS AGREEMENT, made and entered into this 20<sup>th</sup> day of JUNE, A.D. 1974, by and between OUTBOARD MARINE CORPORATION, a Delaware Corporation with its corporate office at 100 Sea Horse Drive, Waukegan, Illinois 60085, hereinafter referred to as "CORPORATION", and NORTH SHORE GAS COMPANY, an Illinois Corporation, 3001 Grand Avenue, Waukegan, Illinois 60085, hereinafter referred to as "LICENSEE".

WITNESSETH:

The CORPORATION for and in consideration of the terms, covenants, agreements and conditions hereinafter contained on the part of the LICENSEE to be made, performed, kept and observed by these presents, does give and grant unto LICENSEE, but without warrenty, subject to the exceptions, reservations, conditions, limitations and provisions hereinafter set forth, the right and privilege to install, operate, maintain, repair, replace and remove a 12-inch gas main, hereinafter referred to as facility, in, under and across CORPORATIONS property located in the South half of Section 15 and the North half of Section 22, Township 45 North, Range 12, East of the Third Principal Meridian, Waukegan, Lake County, Illinois, said facility is to be along the centerline as shown on the drawing marked "EXHIBIT A", attached hereto and hereby made a part hereof.

The rights and privileges herein granted by CORPORATION are accepted by LICENSEE upon the following terms, covenants and conditions:

FIRST: LICENSEE shall notify CORPORATIONS office at least forty-eight (48) hours in advance, except in case of emergency repairs and in cases of routine inspection and operation, before entering upon said property of CORPORATION to make the herein proposed installation, replacement or removal thereof, in order that the CORPORATION can locate its underground facilities (if any) and have a representative or representatives present at such time or times if it so desires and LICENSEE agrees that all work in said property shall be done to the satisfaction of said representative or representatives of said CORPORATION.

SECOND: LICENSEE agrees that said facility will be installed in CORPORATIONS property in strict conformity with said "EXHIBIT A" attached hereto. Any proposed changes in said plans, before or after installation, shall be submitted to CORPORATION for its written approval and no work shall be commenced until such

1677453

Prepared By:  
ROBERT S. BURNS, Attorney  
122 So. Michigan Avenue  
Chicago, Illinois 60603

written approval has been obtained.

THIRD: The rights herein are given subject to any use now made of said property by CORPORATION, its grantees, licensees and lessees, and should CORPORATION desire to make any use of said premises hereafter with which said facility will in any manner interfere, LICENSEE agrees that it will, at its sole cost and expense, within one hundred and twenty (120) days after receiving written notice from CORPORATION, make such changes in said facility as, in the judgment of CORPORATION, may be required to avoid interference with the use or proposed use of its property. LICENSEE agrees to relocate said facility to another location designated by CORPORATION in said property acceptable to LICENSEE.

FOURTH: LICENSEE shall indemnify, save and hold harmless the CORPORATION, its employees, agents and assigns free and harmless from any and all damages, costs and liabilities, including defense of lawsuits and claims which may in any way result from any occurrence as a result of the activity of the LICENSEE, its employees, agents or assigns.

FIFTH: LICENSEE agrees to restore the surface of said CORPORATIONS property, in connection with said facility, damaged by the construction, installation, operation, maintenance, repair, renewal or removal of such facility or related facilities, to the condition of said property immediately before such damage occurred and LICENSEE shall also be obligated to replace trees, shrubs or fences that are damaged or destroyed by the construction, installation, operation, maintenance, repair, renewal or removal of said facility and related facilities.

SIXTH: LICENSEE agrees that there shall be no impairment of natural or installed drainage facilities occasioned by the installation, repair, maintenance or removal of said facility.


SEVENTH: Termination of this agreement shall be to the satisfaction of both the CORPORATION and the LICENSEE.

EIGHTH: The terms "CORPORATION" and "LICENSEE" wherever used in this instrument are intended in each instance to include the respective successors and assigns of CORPORATION or LICENSEE, whichever the case may be, and all of the terms and provisions of this instrument shall inure to the benefit of and be binding upon the respective successors and assigns of CORPORATION and LICENSEE.

IN WITNESS WHEREOF, the parties hereto have caused this instrument to be executed in their respective names by their respective officers or representatives all as of the day and year first above written.


OUTBOARD MARINE CORPORATION

BY *Earl R. Runk*  
Vice President

  
*John N. Sagar*  
Assistant Secretary

NORTH SHORE GAS COMPANY

BY *L. B. Ballantyne*  
Vice President

  
*Tom [Signature]*  
Assistant Secretary

Approved As To Form  
*14B* *RJF*

1677453

DOG  
FILED FOR RECORD IN RECORDERS  
OFFICE LAKE COUNTY, ILLINOIS

MAR 27 74 11 32 AM

✓ *Frank B. Rustra* ✓  
FRANK B. RUSTRA RECORDER

↓  
Mail To  
North Shore Gas Co.  
3001 Grand Ave.  
Waukegan, Ill.  
Attn: Engineering Dept. *R*

209 Madison Street  
Waukegan, Illinois

March 3, 1956

Johnson Motors  
Waukegan, Illinois

Attention: Mr. P. Ellingson, *Plant Eng*

Gentlemen:

In accordance with our telephone conversation I am listing the cost figures as submitted to us by our contractor.

If we were to lay the line inside the fence, the cost would be as follows:

Digging cost	\$ 4.25 lineal foot
1,800 sq. yards black top	12.50 square yard
26 square yards concrete	14.50 square yard
230 lineal feet of concrete sawing	2.50 lineal foot

If we were to lay the line outside the fence, the cost would be as follows:

Digging cost	\$ 3.15 lineal foot
34 square yards black top	12.50 square yard

Both would have to have about 10 yards of gravel at \$6.75 per yard and an approximate footage of 1,400 feet of 6" pipe would be required; our unit cost on 6" pipe is \$1.59 per foot.

In the above I have not quoted tape cost for wrapping joints or patching, however, this would be a minor cost.

Assuming 1,400 feet of pipe if we construct outside the fence, the approximate cost, using the above figures, would be \$7,128.50, while inside construction would be approximately \$10,985.00.

If any further information is desired, please do not hesitate to contact us.

Yours very truly,

O. F. Rogers  
Superintendent  
Production and Engineering

OFF/e

DRAFT

Mr. P. E. Ellingsen, Maintenance Engineer  
Johnson Motor Company  
Waukegan, Illinois

Dear Mr. Ellingsen:

Our summation of the various conferences which we have had with you regarding the responsibility as to the cost of relocating the main on your property is as follows:

1. You have already admitted the validity and responsibility of an easement by paying for the change in location of the main, which occurred in 1952.
2. We have been advised that it is a violation of any easement to build a building or an obstruction of any type which would either hinder or deny free access to such an easement.
3. In Articles, 4, 5, and 6 where the word "removal" appears, it refers strictly to the necessity of removal in the form of necessary repair work.

In view of the foregoing observations, we believe it is the responsibility of Johnson Motor Company to bear the cost of the relocation of the main in question.

Yours very truly,

*AK*

*This letter was a rough draft & was to be submitted to Hall for legal approval, however, Ellingsen now (7-3-56) does not believe this necessary. Originally he believed this letter advisable in order to show his superiors our reasons & reasons for Johnson Motors being the cost of moving the main.*  
*AK*

# Johnson MOTORS

A DIVISION OF OUTBOARD MARINE & MANUFACTURING COMPANY • WAUKEGAN, ILLINOIS



March 13, 1956

Mr. O. F. Rogers  
North Shore Gas Company  
209 Madison Street  
Waukegan, Illinois

Dear Mr. Rogers:

I have discussed your proposal of March 3, addressed to Mr. Ellingson, with him, and would like to advise that the re-routing of the present gas main must be done and work should be started as soon as possible.

In view of the fact that there is approximately a \$4,000 saving in the construction cost to re-route this line around the outside of our fence, we would like you to proceed on this basis. Obviously, this hinges on whether or not the E. J. & E. R. R. Company will permit an easement for this work, since the pipe will be erected on their property.

I have discussed this whole matter with our legal advisor, Mr. J. M. Gross and he in turn discussed it with Mr. Fred Fisher of E. J. & E., and they advised that the request for the easement should originate with the North Shore Gas Company to E. J. & E.

At the time of the request you should submit a sketch for plot plan, showing the property and where the main will run.

After securing the easement, I would appreciate confirmation of the fact before work is started.

Very truly yours,

JOHNSON MOTORS

Vice-President and  
Division Manager

J. L. Rayniak  
rb

1402' 6" Pipe @ 1.57 = 2224.00  
 1400' x 3.15 = 4410.00  
 1400' x 4.25 = 425.00  
 150' ~~By 26~~ B.T. @ 1.20 = 180.00  
 26" " Line @ 14.50 = —  
 230' Sawing @ .50/d" = —  
 1040' grade @ 6.75/yd 675.00  
7128.50

2224.00  
 4410.00  
 425.00  
 180.00  
 377.00  
 115.00  
 675.00  
10986.00





McL...

Small Cell -

Small Tray

\$4.25 per lot #  
1st 29 yd. 1/2" Tw @ 12.50  
26 " " 1/2" Tw @ 14.50  
230 lbs. for 100 yd.

@ \$4.50 per lot.

Outside Fence

\$3.15 per lot #  
34 29 yd. 1/2" Tw @ 12.50

Both ends 1/2" Tw  
about 10 yd. 1/2" Tw  
@ \$6.50 per lot #  
V.C.



# NORTH SHORE GAS COMPANY

DEPARTMENTAL CORRESPONDENCE

To: Mr. C. J. Mulholland

From: Wm. J. Wuestenfeld

Subject:

Date: March 16, 1949

We are attaching hereto easement granted by the Outboard, Marine & Manufacturing Company to the North Shore Gas Company for permission to lay a six inch gas main on their property in the vicinity of the North Plant. This easement has been recorded.

*Wm. J. Wuestenfeld*  
Wm. J. Wuestenfeld

WJW:v  
Att.

This Indenture made this 8<sup>th</sup> day of March, 1949, by and between OUTBOARD, MARINE & MANUFACTURING COMPANY, a Delaware corporation (hereinafter called the "Grantor") and NORTH SHORE GAS COMPANY, an Illinois corporation (hereinafter called the "Grantee"),

WITNESSETH: THAT,

WHEREAS, the Grantor is the owner of certain property in the North West quarter of Section 22, Township 45 North, Range 12 East of the Third Principal Meridian, in Lake County, Illinois, described as follows (hereinafter referred to as "Grantor's property"):

Beginning at a point in the North line of said Section 22, 10 feet Easterly from, measured at right angles to, the center line of the most Easterly main lead track of the Elgin, Joliet and Eastern Railway Company as now located across the North West quarter of said Section 22, said point being 576 feet, more or less, East of the North West corner of said Section 22 measured along the North line of said Section 22; thence continuing East along the North line of said Section 22, 357 feet to a point; thence Southerly along a straight line which makes a Southwesterly angle of 85 degrees 30 minutes from said North line of said Section 22, 498.4 feet to a point on the Northerly line of the strip of land 20 feet in width which the Elgin, Joliet and Eastern Railway Company conveyed to the Outboard Marine and Manufacturing Company by special warranty deed dated January 2, 1948 and recorded in deed record book No. 863 on page 417; thence Westerly along the Northerly line of said strip of land 20 feet in width 350 feet to a point 10 feet Easterly from the center line of the track leading into the Southerly side of Slip No. 3, measured at right angles to the tangent of curve of said tract, said point last mentioned also being 551.4 feet, more or less East of the West line of said Section 22, measured at right angles thereto; thence Northerly parallel to and 10 feet Easterly from the center line of said track leading into the Southerly side of said Slip No. 3 and said most Easterly main lead track, as now located, 458.4 feet more or less to the point of beginning;

and

WHEREAS, the Grantee desires to lay, construct, operate, maintain and repair a six inch (6") gas main across Grantor's property in order to supply gas to Grantor's building on Grantor's property and in order to provide future gas supply to other properties, including the property of Grantor on the lake front, and the Grantor is willing to grant to the Grantee a perpetual easement for that purpose subject to the terms and conditions hereinafter set forth;

NOW, THEREFORE, for and in consideration of the sum of Ten Dollars (\$10.00) and other valuable consideration in hand paid by the Grantee to the Grantor, receipt of which is hereby acknowledged, the Grantor hereby gives and grants unto the Grantee a perpetual easement to lay, construct, operate, maintain and repair a six inch (6") gas main across the Grantor's property for the purposes above mentioned upon the following terms and conditions:

1. Subject to the right of relocation hereinafter provided, the six inch (6") gas main shall be laid across Grantor's property as indicated in the dotted red line on the plat attached hereto which is hereby made a part of this Indenture.

2. It is understood and agreed that the title to the six inch (6") gas main laid across Grantor's property shall at all times remain in Grantee.

3. The gas main shall be maintained at a minimum depth of four (4) feet below the floor level of the building on Grantor's property.

✓ 4. Grantee covenants to maintain the gas main in good condition, and shall, upon obtaining in each case the prior ~~written~~ <sup>oral</sup> consent of Grantor, its successors or assigns, have access to the gas main for the purpose of inspection, repair, maintenance or removal thereof.

✓ 5. All work in connection with the construction, maintenance, renewal and repair of said gas main and all equipment used therewith, including replacements caused by the utilization of Grantor's property, shall be performed by and all cost and expense to be incurred shall be borne by and paid by Grantee. All work done shall be in accordance with accepted practices for such services and shall meet local conditions applicable to design and construction.

✓ 6. Grantee, its successors and assigns, shall indemnify and hold harmless the Grantor, its successors and assigns, against any costs, expenses, suits, loss, damage, injury or liability of any kind whatsoever arising out of the construction, operation, maintenance, repair or removal of said gas main or the use of the right herein granted.

✓ 7. The Grantor reserves and shall have the right at any time or from time to time to change the location of the gas main to any other location on Grantor's property, but in such event the location of the gas main shall be so changed at the expense of the Grantor and such relocated gas main shall continue to begin and end at the beginning and ending points indicated on the plat attached hereto. Upon any such relocation the easement hereby granted

as to the old location shall cease and shall be deemed to have been released, and the easement shall thereafter be deemed to exist only in respect of such relocated gas main.

8. Grantee does hereby release and forever waive any and all rights granted to or acquired by it under an agreement relating to gas mains between Elgin, Joliet and Eastern Railway Company (a prior owner of Grantor's property) and Grantee, dated May 2, 1929, in so far as such rights or said agreement pertains to Grantor's property above described and all other property in Lake County, Illinois, now owned by Grantor.

9. All of the provisions herein contained shall bind and inure to the benefit of the successors and assigns of the parties hereto.

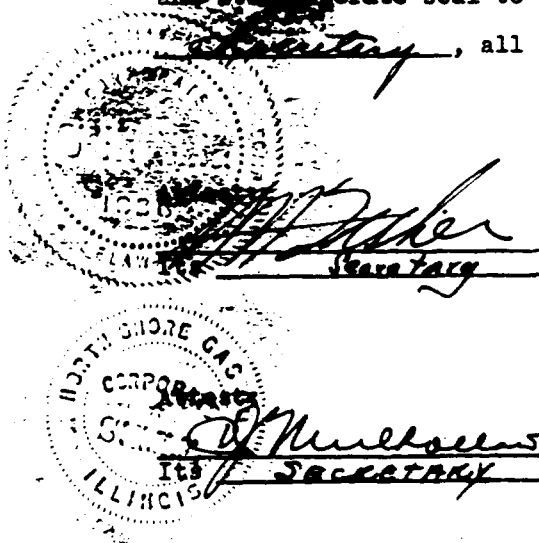
IN WITNESS WHEREOF, said Outboard, Marine & Manufacturing Company has caused this Indenture to be executed in its name and on its behalf by its Vice-President and its corporate seal to be hereunto affixed and attested by its Secretary, and said North Shore Gas Company has caused this Indenture to be executed in its name and on its behalf by its President and its corporate seal to be hereunto affixed and attested by its Secretary, all on the day and year first above written.

OUTBOARD, MARINE & MANUFACTURING COMPANY

By J. J. [Signature]  
VICE-PRESIDENT

NORTH SHORE GAS COMPANY

By [Signature]  
Its PRESIDENT



STATE OF ILLINOIS }  
COUNTY OF LAKE } SS

I, E. C. Hollmann a notary public  
in and for the said County in the State aforesaid, do  
hereby certify that P. G. Danner and  
H. D. Fisher, personally known to me  
to be the same persons whose names are, respectively, as  
Vice President and Secretary of  
Outboard, Marine & Manufacturing Company, a Delaware cor-  
poration, subscribed to the foregoing instrument, appeared  
before me this day in person and severally acknowledged  
that they, being thereunto duly authorized, signed, sealed  
with the corporate seal, and delivered the said instrument  
as the free and voluntary act of the said corporation and  
as their own free and voluntary act, for the uses and  
purposes therein set forth.

IN WITNESS WHEREOF, I have hereunto affixed my  
signature and notarial seal this 9th day of March,  
1949.

E. C. Hollmann  
Notary Public

My commission expires My Commission Expires Aug. 11, 1949



STATE OF ILLINOIS }  
COUNTY OF LAKE } SS

I, J. R. Hess, a notary public  
in and for the said County in the State aforesaid, do  
hereby certify that A. W. Connor and  
C. J. Mulholland, personally known to me  
to be the same persons whose names are, respectively, as  
President and Secretary  
of North Shore Gas Company, an Illinois corporation, sub-  
scribed to the foregoing instrument, appeared before me  
this day in person and severally acknowledged that they,  
being thereunto duly authorized, signed, sealed with the  
corporate seal, and delivered the said instrument as the  
free and voluntary act of the said corporation and as their  
own free and voluntary act, for the uses and purposes therein  
set forth.

IN WITNESS WHEREOF, I have hereunto affixed my  
signature and notarial seal this 8 day of March,

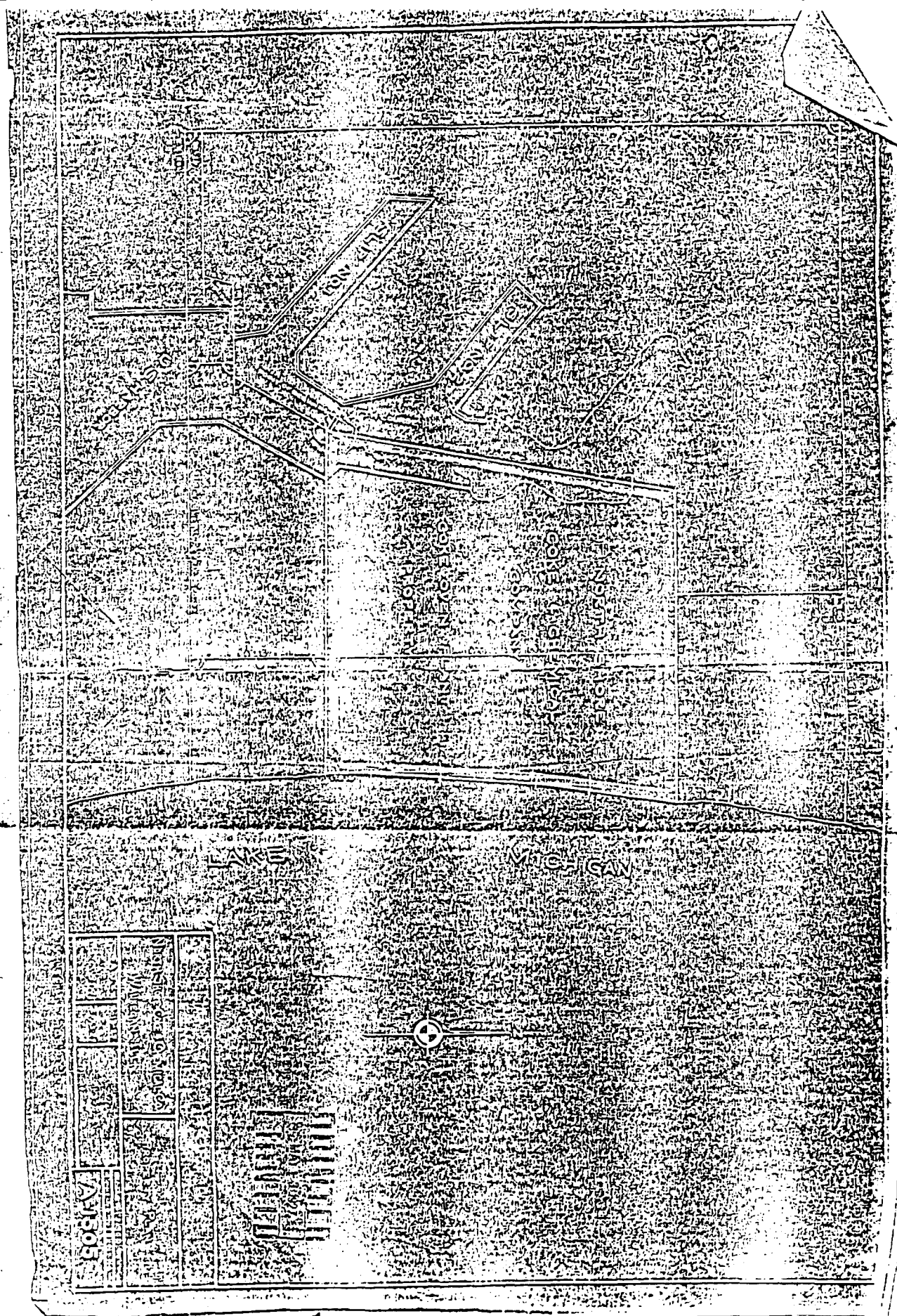


J. R. Hess  
Notary Public

My commission expires Nov 4 1956

State of Illinois } ss. No. 665456  
Lake County }  
Filed for record MAR 10 A.D.  
1949 at 2:55 o'clock P.M. and  
duly recorded in Book 915  
of RECORDS Page 76  
Georg H. Fredbeck  
Recorder





THIS INDENTURE Made this \_\_\_\_\_ day of \_\_\_\_\_, 1949,  
between JOHNSON MOTORS, DIVISION OF OUTBOARD MARINE AND MANUFACTURING COMPANY, a  
Delaware corporation, duly authorized to do business in the State of Illinois,  
First Party, for and in consideration of the sum of One Dollar (\$1.00) and  
other good and valuable consideration to it paid by the NORTH SHORE GAS COMPANY,  
an Illinois corporation, of 209 Madison Street, Waukegan, Illinois, Second Party,  
the receipt whereof is hereby acknowledged, does hereby grant unto the Second  
Party, its successors and assigns, a perpetual easement and right-of-way to lay  
and maintain a six inch (6") gas pipe across Tract "A" of First Party's property,  
Tract "A" being a tract of land lying in the Northwest quarter of the Northwest  
quarter of Section 22, Township 45 North, Range 12 East of the Third Principal  
Meridian, Lake County, Illinois, described as follows:

Tract "A": Beginning at a point in the North line of said  
Section 22, that is 10 feet Easterly from, measured at  
right angles to the center line of the most Easterly main  
lead track of the Elgin, Joliet and Eastern Railway Company,  
as now located across said Section 22 (said point of  
beginning being 576 feet east of the Northwest corner of  
said Section 22; thence Southerly along a line drawn parallel  
to and 10 feet Easterly from said center line of main line  
lead track and the center line of the spur track leading to  
Slip No. 3, 458.4 feet, more or less, to a point in the  
Northerly line of the strip of land, 20 feet in width, which  
the Elgin, Joliet and Eastern Railway Company heretofore  
conveyed to the Outboard Marine and Manufacturing Company by  
quit claim deed dated January 2, 1948, and recorded in Deed  
Record Book No. 863 on Page 417 of the Office of Recorder of  
Deeds of Lake County, Illinois; thence Easterly along the  
Northerly line of said strip of land 20 feet in width, 350  
feet to a point; thence in a Northerly direction 498.4 feet,  
more or less, to a point on the North line of said Section  
22, 357 feet East of the place of beginning; thence West along  
said North line of said Section 22, 357 feet to the place of  
beginning;

said six inch (6") main to be laid as indicated in a dotted red line on the  
attached plan and made a part of this Indenture, for a gas supply for the First  
Party's building on Tract "A" and for future supply to First Party's property  
on the lake front, as well as for future supply required by the Second Party,  
upon the following terms and conditions:

1. It is understood and agreed that the title to the said six inch  
(6") gas main in the premises described shall at all times remain in the Second  
Party, its successors and assigns, together with the right at any time to  
replace or remove all or any part thereof.

2. All work in connection with the maintaining, renewing, and repairing of said six inch (6") gas main and all other equipment therewith, including replacements caused by the utilization of First Party's property shall be performed by and all cost and expense to be incurred shall be borne by and paid by Second Party, its successors and assigns. All work done shall be in accordance with accepted practices for such services and shall meet local conditions applicable to design and construction.

3. Second Party, its successors and assigns, shall at all times indemnify and hold harmless First Party, its successors and assigns, against any costs, expenses, suits, loss, damage, injury or liability of any kind whatsoever arising out of the construction, maintenance and use of the right herein granted.

IN WITNESS WHEREOF the First Party has caused this Indenture to be executed the day and year first above written.

ATTEST:

JOHNSON MOTORS, DIVISION OF OUTBOARD  
MARINE AND MANUFACTURING COMPANY

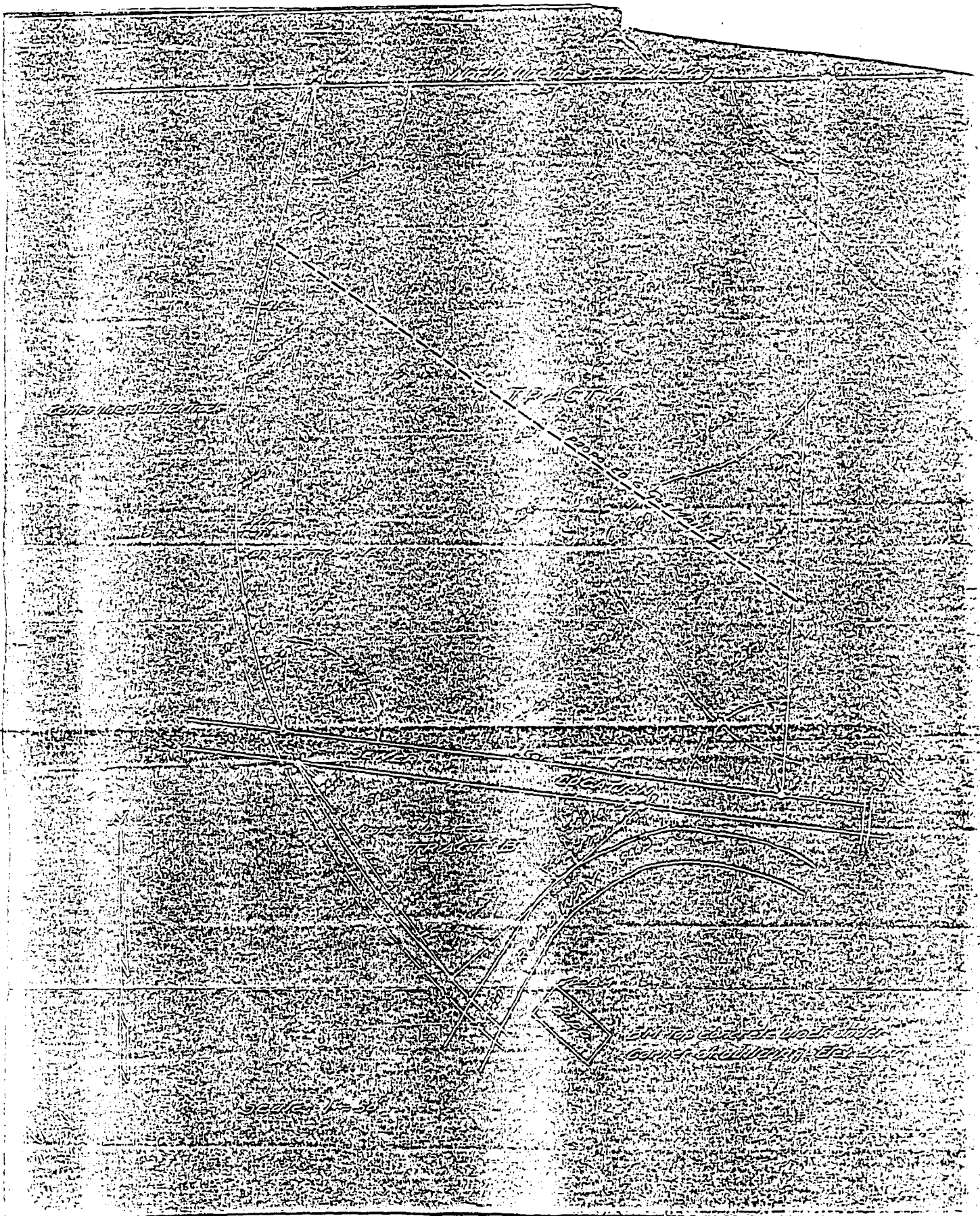
BY: \_\_\_\_\_

STATE OF ILLINOIS) )  
COUNTY OF LAKE ) SS.

I, \_\_\_\_\_, a Notary Public in and for said County in the State aforesaid, do hereby certify that \_\_\_\_\_ President of Johnson Motors, Division of Outboard Marine and Manufacturing Company, a Delaware corporation, and \_\_\_\_\_ Secretary of said corporation, personally known to me to be the same persons whose names are subscribed to the foregoing instrument as such \_\_\_\_\_ President and Secretary, respectively, appeared before me this day in person and acknowledged that they signed and delivered the said instrument as their own free and voluntary act and as the free and voluntary act of said corporation for the uses and purposes therein set forth; and the said \_\_\_\_\_, Secretary, then and there acknowledged that he, as custodian of the corporate seal of said corporation, did affix the corporate seal of said corporation to said instrument as his own free and voluntary act and as the free and voluntary act of said corporation for the uses and purposes therein set forth.

GIVEN under my hand and notarial seal this \_\_\_\_\_ day of \_\_\_\_\_, A.D. 1949.

\_\_\_\_\_  
Notary Public





North line of Sec 16-15-25

East line of Sec 16-15-25

TRACT A

DRIP ST. 1/2

SEWER

TRACT B

East line of Sec 16-15-25  
Center of Ditch 1/2

Scale 1"=50'

Exhibit W

THE UNIVERSITY OF CHICAGO

MANUFACTURING STRUCTURE  
AND PATTERN OF  
WAUKEGAN-NORTH CHICAGO

---

*A dissertation submitted to the faculty  
of the Division of the Physical Sciences in candidacy  
for the degree of Doctor of Philosophy*

DEPARTMENT OF GEOGRAPHY

RESEARCH PAPER NO. 46

*By*

G. Munir Ahmed, Ph.D.

CHICAGO - ILLINOIS

FEBRUARY, 1957

Railway, which is becoming increasingly industrial in character (Fig. 6).

The railroads, primarily the Elgin, Joliet and Eastern and the Chicago and North Western, have been the dominant factors in the present morphology of industrial land uses in Waukegan-North Chicago. The industries have located as close as possible to the railroads. This situation explains the linear character of the industrial belt of the study area. Similarly, a linear belt along the North Shore Line is also in the making. The entire industrial structure has a southern base where all three railroads come closest to one another. Two industrial belts branch out from this base. One of them takes a north-northeasterly direction while the other extends due north. The northeasterly belt is the more highly developed and concentrated, and it lies on the lake plain. The northern belt has only a spotty industrial development, primarily of a light industrial character. The northeasterly industrial belt closely follows the Elgin, Joliet and Eastern and the Chicago and North Western; the northern industrial belt follows the Chicago, North Shore and Milwaukee.

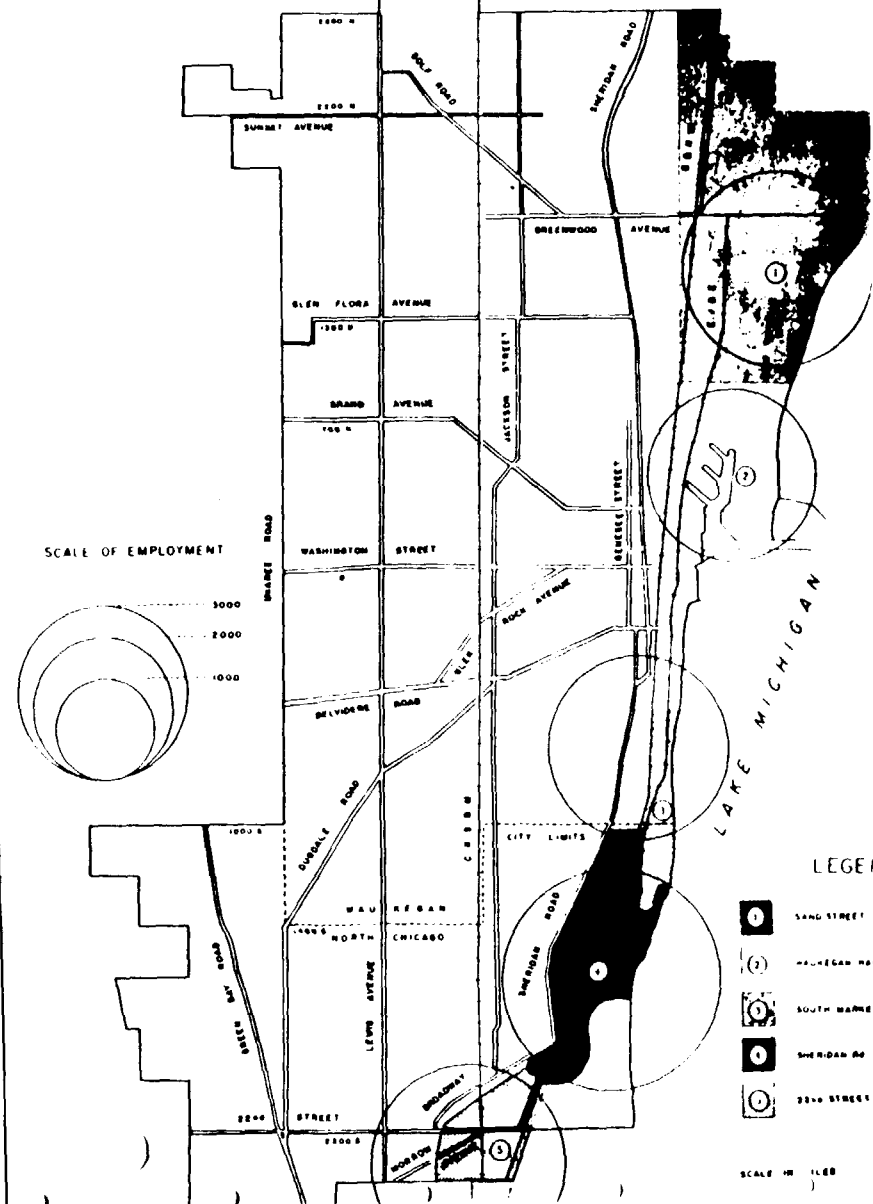
The lake plain industrial belt may be divided into several industrial clusters (Fig. 7). The division is intended for purposes of closer study.<sup>1</sup> The industrial clusters are: (1) Sand Street-Greenwood Avenue Area, (2) Waukegan Harbor Area, (3) South Market Street-Tenth Street Area, (4) Sheridan Road-Foss Park Avenue Area, and (5) Twenty-Second Street Area.

Sand Street-Greenwood Avenue Area.--Areally, the Sand Street-Greenwood Avenue Area is the largest industrial cluster of Waukegan-North Chicago. The chief industries included in it are: Johns Manville, Public Service Company, Griess-Fleger, Pacific Steel Boiler, and North Shore Gas Company. A considerable portion of the northern part of the area included in this cluster is outside the Waukegan city limits. Generally, the industries located in this area are large ones. On the whole, this area does not present a crowded picture of industrial land uses.

Waukegan Harbor Area.--The Waukegan Harbor industrial area extends to the north and west of Waukegan Harbor. The chief indus-

<sup>1</sup>The area enclosed within an industrial concentration does not necessarily include the total area owned and held by the industries located within such a concentration. Accordingly the lines of demarcation of the various industrial concentrations should not be construed as indicative of the ownership of the area by the industries contained within the industrial concentrations.

# WAUKEGAN-NORTH CHICAGO INDUSTRIAL CLUSTERS AND MANUFACTURING EMPLOYMENT



tries of this area are Johnson Motors, Mosow Screw, Chevrolet Saginaw Foundry, and Blatchford Calf Meal Company. The cluster is confined by the bluff to the west and Lake Michigan to the east. It enjoys proximity to the Central Business District of Waukegan as well as to Waukegan Harbor; at the same time, it faces problems of traffic congestion and railroad crossings.

Sand Street needs to be improved to function more efficiently as a highway. Also, Pershing Drive, which is the only highway to reach the North Beach and the industries (Johnson Motors and Chevrolet Saginaw Foundry), in view of its present traffic, justifies any program to improve it.

South Market Street-Tenth Street Area.--This area extends east of the railroads from 600 South to 1300 South. The South Market Street Area is highly concentrated with industrial land use. Most of the industrial buildings are old and their appearances show lack of proper upkeep. At the same time increasing rehabilitation is in progress in the area. The new and attractive building of the Vascoloy-Ramet Corporation looks impressive and offers a good example of rejuvenation. South Market Street suffers from the disadvantages of being a very narrow strip of land, bound on the east by Lake Michigan and on the west by the railroads and the cemeteries. This circumstance further adds to the concentration of the industrial land use.

Just south of Market Street, and on the lake shore, lies the American Steel and Wire Mill, which stretches from about 850 South to about 1370 South.<sup>1</sup> On the other side of the Chicago and North Western, along Tenth Street lies another big industry: United States Envelope Company. The area between the American Steel and Wire Mill and Sheridan Road is owned by industrial interests and held for new plants or future expansion.

Sheridan Road-Foss Park Avenue Area.--This area lies east of Sheridan Road from about 1300 South to about 2000 South. Foss Park limits the eastern expansion of the area. It includes the Abbott Laboratories, the largest industrial establishment of the Waukegan-North Chicago area. Other industries of this area are Houdaille-Hershey Corporation, Cyclone Fence, National Press, and a few smaller ones. Industries bordering the Foss Park Avenue are attractively maintained; an irregular street pattern gives a break from the ubiquity of the gridiron. Abbots, with its clus-

<sup>1</sup>The area actually occupied by Mill is included in this cluster.

American Steel and Wire

ter of buildings and its extensive parking lots, however, presses the passers-by on Sheridan Road. In general, the tries do not appear to be crowded.

Twenty-Second Street Area.--This area extends from 2100 South to 2400 South, and from the west of Sheridan Road about 1800 West. This is the southernmost industrial cluster. Its eastern and southern expansion is blocked by the Great Naval Training Station, though the cluster's southernmost extension lies outside the southern city limits of North Chicago.

The chief characteristic of this area is the presence of a network of railroads which almost encircles the whole area on three sides. Areally a small division, it is well represented by a number of industries, big and small. Morrow Avenue presents an attractive appearance. Also, Twenty-Second Street is a major east-west highway.

Fansteel Metallurgical Corporation extends from Sheridan Road to Commonwealth Avenue along Twenty-Second Street with minor breaks in its continuity. National Cranberry Association and Amco Tools are located on Commonwealth Avenue north of Second Street; the Chicago Hardware Foundry is located on Commonwealth Avenue, south of Twenty-Second Street. On Morrow Avenue the big industries are the Deep Freeze Appliance Division and Goelitz Confectionery.

Industrial land use along the Chicago, North Shore and Milwaukee Railroad is not continuous north of the last discussed industrial cluster, and the spotty industrial land use does not contain any significant industrial concentrations.

The above discussion reveals that the lake plain industrial belt is in itself composed of the smaller groups of industrial clusters. The big industries are the main stabilizers of industrial location and development in each of the groups. The small industries, however, provide variety in the industrial structure both with respect to size and the nature of the products.

Table 6 further illustrates the characteristics of the industrial clusters.

Table 7 presents information relative to the employment densities of the census group of industries as of the Summer of 1950.

#### Pattern of Land Uses

One of the striking features of the present land-use pattern of Waukegan-North Chicago is the parallel, linear nature of the industrial clusters. The clusters are generally oriented along the major transportation routes, particularly the railroad and the highway.



Exhibit X

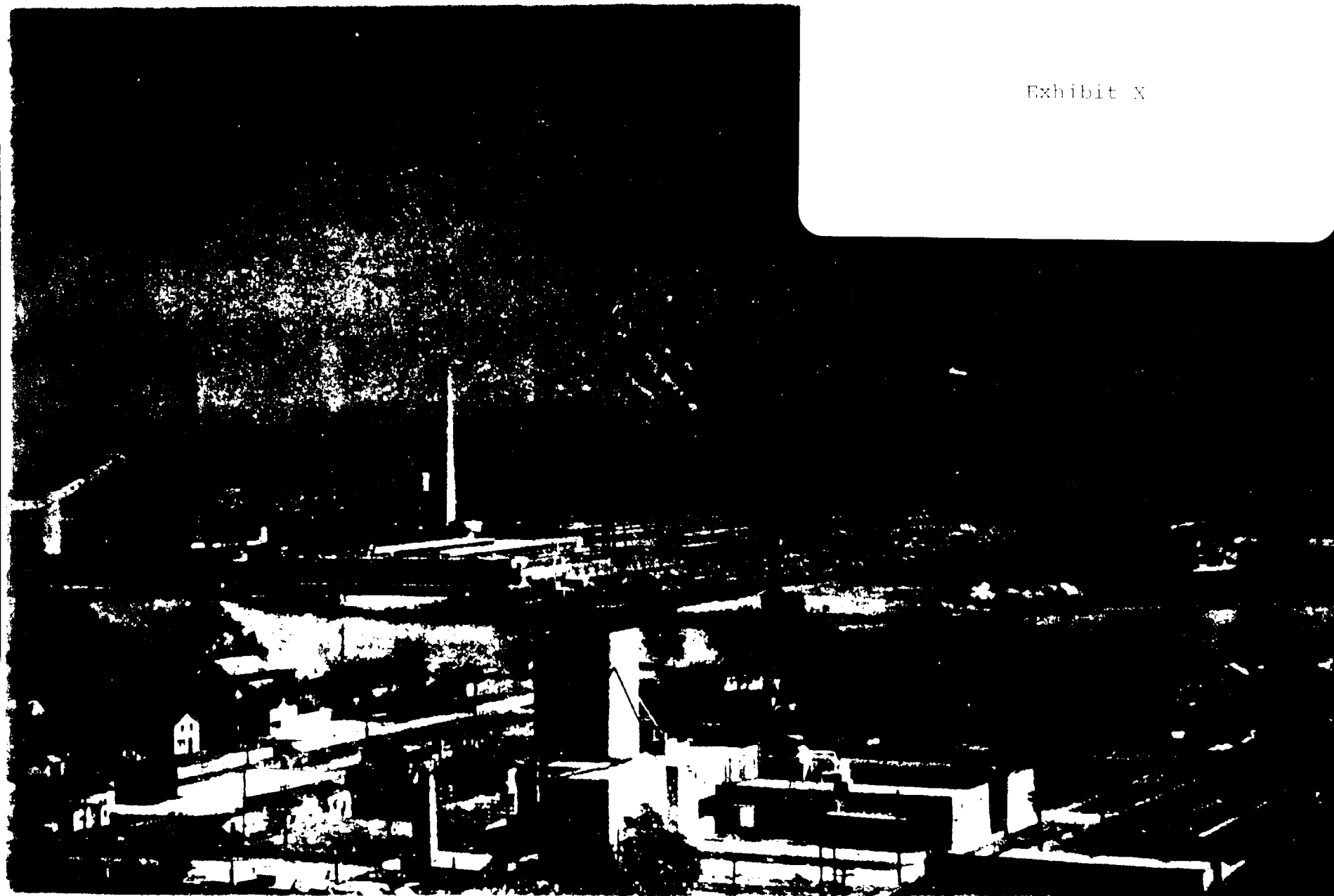


Fig. 23.--A View Looking Northeast, Showing a Close-up of a Section of the Industrial Cluster of "Waukegan Harbor Area."

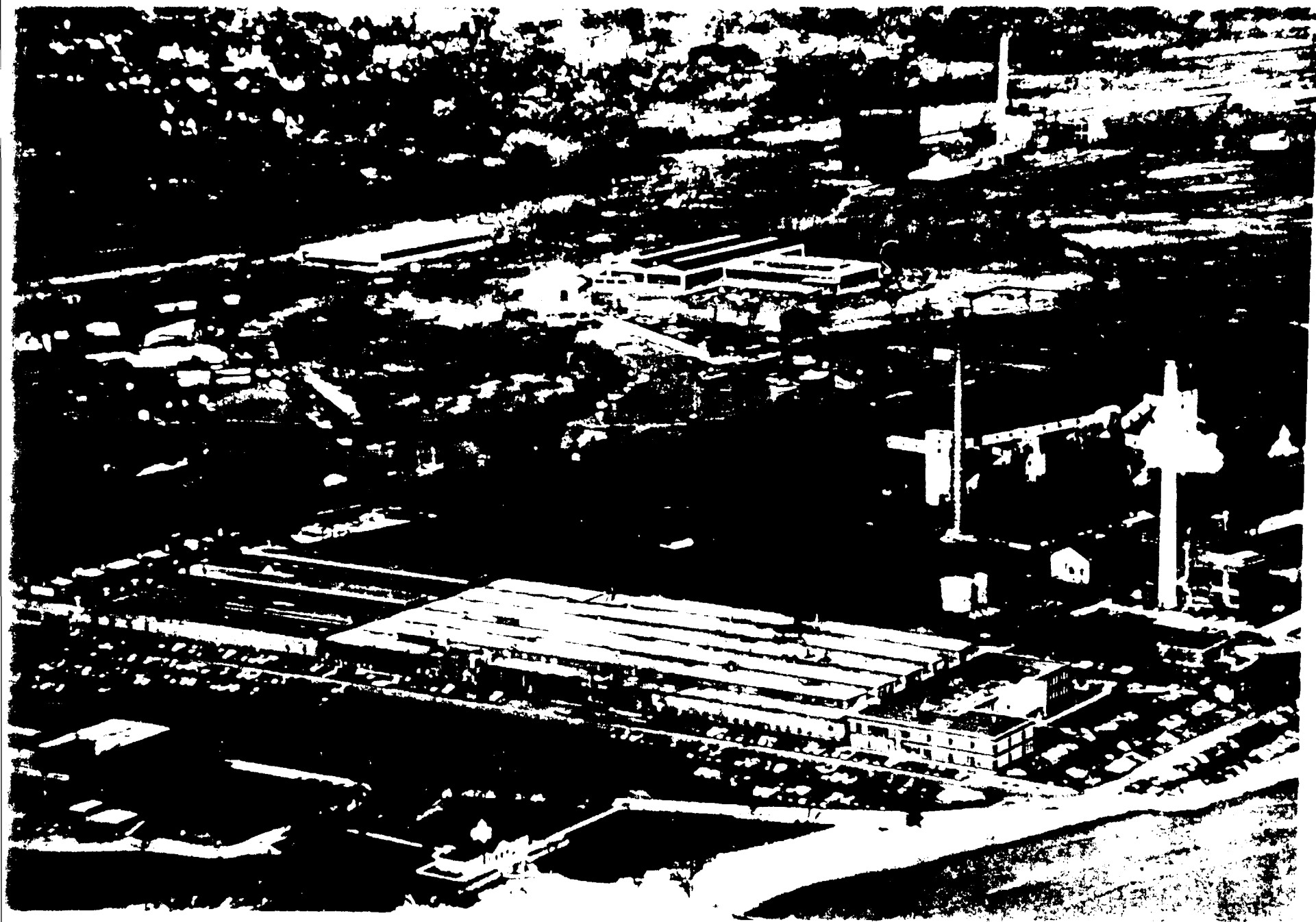


Fig. 22.--A View Looking Northwest, from Lake Michigan. Johnson Motors Is Seen in the foreground. The Photograph Portrays the "Industrial Cluster of Waukegan Harbor Area."



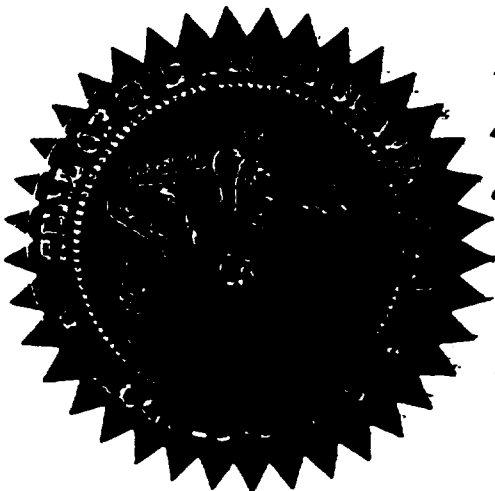
Fig. 20.--A View Looking Northeast, Showing Part of the Business District, the Railroads and the Waukegan Harbor.



**To all to whom these Presents Shall Come, Greeting:**

*I, Jim Edgar, Secretary of State of the State of Illinois,  
do hereby certify that*

THE FOLLOWING AND HERETO ATTACHED IS A TRUE  
COPY OF THE Articles of Incorporation and all Amendments thereto, to date  
including the latest Change of Registered Agent and Registered Office of  
NORTH SHORE GAS COMPANY, \*\*\*\*\*



**In Testimony Whereof,** *I hereto set  
my hand and cause to be affixed the Great Seal of  
the State of Illinois this* 24th  
*day of* September *A. D., 19* 84.

*Jim Edgar*  
\_\_\_\_\_  
SECRETARY OF STATE

Certificate Number \_\_\_\_\_

1 - 12



**To all to whom these Presents Shall Come, Greeting:**

**Whereas**, Articles of Incorporation duly signed and verified of  
**LAKE GAS COMPANY**

have been filed in the Office of the Secretary of State, on the 7th  
day of October A. D. 19 63, as provided by "THE BUSINESS  
CORPORATION ACT" of Illinois, in force July 13, A. D. 1933.

Now Therefore, I, **CHARLES F. CARPENTIER**, Secretary of State of the State of Illinois,  
by virtue of the powers vested in me by law, do hereby issue this certificate of  
incorporation, and attach thereto a copy of the Articles of Incorporation  
of the aforesaid corporation.

**In Testimony Whereof**, I hereto set my hand and cause to  
be affixed the Great Seal of the State of Illinois,  
Done at the City of Springfield this 7th  
day of October A. D. 19 63 and  
of the Independence of the United States  
the one hundred and 88th

(SEAL)



SECRETARY OF STATE

FORM B

BEFORE ATTEMPTING TO EXECUTE THESE BLANKS BE SURE TO READ CAREFULLY  
THE INSTRUCTIONS ON THE BACK THEREOF.

(THESE ARTICLES MUST BE FILED IN DUPLICATE)

STATE OF ILLINOIS,

COOK COUNTY } ss.

To CHARLES F. CARPENTIER, Secretary of State:

(Do not write in this space)  
Date Paid 10-7-63  
Initial License Fee \$ 50  
Franchise Tax \$ 7.50  
Filing Fee \$ 70  
Clerk

We, the undersigned,

Name	Number	Street	City	State
William P. O'Keefe	122	South Michigan Avenue,	Chicago,	Illinois
Philip B. Hill	122	South Michigan Avenue,	Chicago,	Illinois
Hugh A. Zimmerman	122	South Michigan Avenue,	Chicago,	Illinois

being natural persons of the age of twenty-one years or more and subscribers to the shares of the corporation to be organized pursuant hereto, for the purpose of forming a corporation under "The Business Corporation Act" of the State of Illinois, do hereby adopt the following Articles of Incorporation:

ARTICLE ONE

The name of the corporation is: LAKE GAS COMPANY

ARTICLE TWO

The address of its initial registered office in the State of Illinois is: 209 Madison  
Street, in the City of Waukegan ( ) County of Lake and  
the name of its initial Registered Agent at said address is: Edwin M. Taber

ARTICLE THREE

The duration of the corporation is: Perpetual

## ARTICLE FOUR

The purpose or purposes for which the corporation is organized are:

To construct, own, lease and operate a plant or plants for manufacturing, producing, generating, storing and furnishing gas, electricity, various fluids and other forms of energy and to sell and distribute the same through pipes, conductors, conduits or otherwise in liquid or gaseous or other forms for heating, cooling, air conditioning, cooking, lighting, power, and for such other purpose or purposes as the same now or hereafter may be useable or applicable to and for; and for the production and sale of the by-products connected with or incidental to the operation of said plant or plants and for such other business or purposes as may be connected therewith or pertinent thereto.

To construct, develop, explore for, purchase or otherwise acquire, and to own, hold, maintain and operate pipelines, storage reservoirs, caverns, all other storage facilities, and all other equipment and property suitable, necessary or convenient, incident or pertinent thereto, and to the transportation and storage of natural gas and all other gases in liquid or gaseous form; and to engage in the business of the transportation and storage of all such gases for itself and others.

To buy and sell gas, oil, salt, brine and other mineral solutions and to produce gas and oil; to manufacture, buy, sell, deal in, engage in, conduct and carry on the business of manufacturing, buying, selling, leasing, lending and dealing in goods, wares and merchandise of every class and description, including, but not limited to, machinery, equipment and appliances of all kinds which may be applicable to or used in connection with the production, generation, transmission, distribution, storage, use or consumption of gas, electricity, various fluids and other forms of energy, and to advance its funds in connection with the sale and installation or use of any thereof.

4-1611

## ARTICLE FIVE

PARAGRAPH 1: The aggregate number of shares which the corporation is authorized to issue is 2,000,000, divided into \_\_\_\_\_ classes. The designation of each class, the number of shares of each class, and the par value, if any, of the shares of each class, or a statement that the shares of any class are without par value, are as follows:

Class	Series (If any)	Number of Shares	Par value per share or statement that shares are without par value
Common	-	2,000,000	Without par value

PARAGRAPH 2: The preferences, qualifications, limitations, restrictions and the special or relative rights in respect of the shares of each class are:

None

## ARTICLE SIX

The class and number of shares which the corporation proposes to issue without further report to the Secretary of State, and the consideration (expressed in dollars) to be received by the corporation therefor, are:

Class of shares	Number of shares	Total consideration to be received therefor:
Common	200	\$ 1,000.00 \$ \$ \$ \$

## ARTICLE SEVEN

The corporation will not commence business until at least one thousand dollars has been received as consideration for the issuance of shares.

## ARTICLE EIGHT

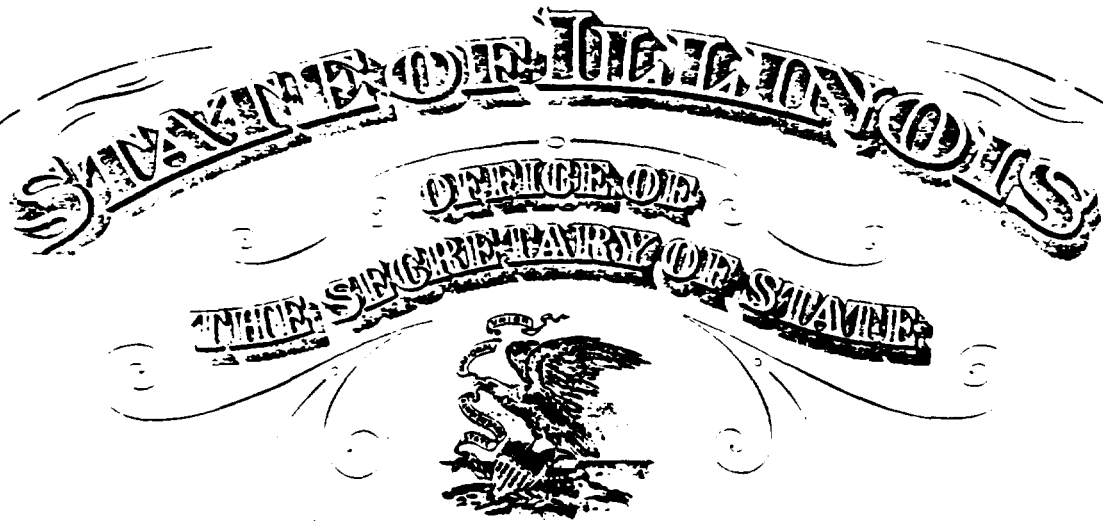
The number of directors to be elected at the first meeting of the shareholders is: Three (3)



**Notary Public**

Certificate Number \_\_\_\_\_

7-1511



**To all to whom these Presents Shall Come, Greeting:**

**Whereas**, Articles of amendment to the Articles of Incorporation duly signed and verified of \_\_\_\_\_  
LAKE GAS COMPANY

have been filed in the Office of the Secretary of State, on the \_\_\_\_\_ 20th  
day of \_\_\_\_\_ December A. D. 1963, as provided by "THE BUSINESS  
CORPORATION ACT" of Illinois, in force July 13, A. D. 1933.

Now Therefore, I, CHARLES F. CARPENTIER, Secretary of State of the State of Illinois,  
by virtue of the powers vested in me by law, do hereby issue this certificate of  
amendment, and attach thereto a copy of the Articles of Amendment to  
the Articles of Incorporation of the aforesaid corporation.

**In Testimony Whereof**, Thereto set my hand and cause to  
be affixed the Great Seal of the State of Illinois.  
Done at the City of Springfield this \_\_\_\_\_ 20th  
day of \_\_\_\_\_ December A. D. 1963 and  
of the Independence of the United States  
the one hundred and \_\_\_\_\_ 88th.

(SEAL)

Charles F. Carpentier

SECRETARY OF STATE

(File in Duplicate)

(Do not write in this space)

Date Paid	12-20-63
License Fee	\$
Franchise Tax	\$
Filing Fee	\$20.00
Clerk	70

**ARTICLES OF AMENDMENT  
TO THE  
ARTICLES OF INCORPORATION  
OF**

**LAKE GAS COMPANY**  
(Exact Corporate Name)

To CHARLES F. CARPENTIER,  
Secretary of State  
Springfield, Illinois

PAID  
DEC 20 1963  
CLERK  
STATE

The undersigned corporation, for the purpose of amending its Articles of Incorporation and pursuant to the provisions of Section 55 of "The Business Corporation Act" of the State of Illinois, hereby executes the following Articles of Amendment:

ARTICLE FIRST: The name of the corporation is:

LAKE GAS COMPANY

ARTICLE SECOND: The following amendment or amendments were adopted in the manner prescribed by "The Business Corporation Act" of the State of Illinois:

The Articles of Incorporation of Lake Gas Company be, and the same hereby are, amended so as to change the name of said Company from Lake Gas Company to North Shore Gas Company. *ik*

9-1611

(Disregard separation into classes if class voting does not apply to the amendment voted on.)

ARTICLE THIRD: The number of shares of the corporation outstanding at the time of the adoption of said amendment or amendments was 200  
\_\_\_\_\_; and the number of shares of each class entitled to vote as a class on the adoption of said amendment or amendments, and the designation of each such class were as follows:

Class	Number of Shares
-------	------------------

-

(Disregard separation into classes if class voting does not apply to the amendment voted on.)

ARTICLE FOURTH: The number of shares voted for said amendment or amendments was 200; and the number of shares voted against said amendment or amendments was none  
The number of shares of each class entitled to vote as a class voted for and against said amendment or amendments, respectively, was:

Class	Number of Shares Voted	
	For	Against

-

(Disregard these items unless the amendment restates the articles of incorporation.)

Item 1. On the date of the adoption of this amendment restating the articles of incorporation, the corporation had \_\_\_\_\_ shares issued, itemized as follows:

Class	Series (If Any)	Number of Shares	Par value per share or statement that shares are without par value
-------	--------------------	---------------------	---

-

Item 2. On the date of the adoption of this amendment restating the articles of incorporation, the corporation had a stated capital of \$ \_\_\_\_\_ and a paid-in surplus of \$ \_\_\_\_\_ or a total of \$ \_\_\_\_\_.

-

(Disregard this Article where this amendment contains no such provisions.)

10-16-11

ARTICLE FIFTH: The manner in which the exchange, reclassification, or cancellation of issued shares, or a reduction of the number of authorized shares of any class below the number of issued shares of that class, provided for in, or effected by, this amendment, is as follows:

-

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

ARTICLE SIXTH: Paragraph 1: The manner in which said amendment or amendments effect a change in the amount of stated capital or the amount of paid-in surplus, or both, is as follows:

-

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

Paragraph 2: The amounts of stated capital and of paid-in surplus as changed by this amendment are as follows:

	Before Amendment	After Amendment
Stated capital.....\$		\$
Paid-in surplus.....\$		\$

-

11-1611

IN WITNESS WHEREOF, the undersigned corporation has caused these Articles of Amendment to be executed in its name by its \_\_\_\_\_ President, and its corporate seal to be hereto affixed, attested by its Secretary, this 16th day of December 19 63.

LAKE GAS COMPANY  
(Exact Corporate Name)

By Roy E. Jones  
its President

PLACE  
(CORPORATE SEAL)  
HERE

ATTEST:  
Wm. McEl  
its Secretary

STATE OF ILLINOIS  
COUNTY OF COOK } ss.

I, Walter J. McElligott a Notary Public, do hereby certify that on the 16th day of December 19 63, Roy E. Jones personally appeared before me and, being first duly sworn by me, acknowledged that he signed the foregoing document in the capacity therein set forth and declared that the statements therein contained are true.

IN WITNESS WHEREOF, I have hereunto set my hand and seal the day and year before written.

PLACE  
(NOTARIAL SEAL)  
HERE

Walter J. McElligott  
Notary Public

Form BCA-69  
Box 4349 File 143

**ARTICLES OF AMENDMENT**  
**to the**  
**ARTICLES OF INCORPORATION**  
**of**  
LAKE GAS COMPANY

**FILED**  
**DEC 21 1963**  
Charles D. [Signature]  
Secretary of State.

**FILE IN DUPLICATE**  
Filing Fee \$20.00  
Filing Fee for Re-Statd Articles \$50.00



**To all to whom these Presents Shall Come, Greeting:**

**Whereas**, Articles of amendment to the Articles of Incorporation duly signed and verified of \_\_\_\_\_

NORTH SHORE GAS COMPANY

have been filed in the Office of the Secretary of State on the \_\_\_\_\_ 12th day of \_\_\_\_\_ March A. D. 1971, as provided by "THE BUSINESS CORPORATION ACT" of Illinois, in force July 13, A. D. 1933.

Now Therefore, I, **JOHN W. LEWIS**, Secretary of State of the State of Illinois, by virtue of the powers vested in me by law, do hereby issue this certificate of amendment, and attach thereto a copy of the Articles of Amendment to the Articles of Incorporation of the aforesaid corporation.

**In Testimony Whereof**, I hereto set my hand and cause to be affixed the Great Seal of the State of Illinois.

Done at the City of Springfield this \_\_\_\_\_ 12th day of \_\_\_\_\_ March A. D. 1971 and of the Independence of the United States the one hundred and \_\_\_\_\_ 95th.



(File in Duplicate)

(Do not write in this space)

Date Paid	3-14-71
License Fee	\$
Franchise Tax	\$
Filing Fee	\$25.00
Clerk	

**ARTICLES OF AMENDMENT  
TO THE  
ARTICLES OF INCORPORATION  
OF**

2581 00

North Shore Gas Company

(Exact Corporate Name)

To ~~RAULX FOWKELX~~ JOHN W. LEWIS,  
Secretary of State  
Springfield, Illinois

The undersigned corporation, for the purpose of amending its Articles of Incorporation and pursuant to the provisions of Section 55 of "The Business Corporation Act" of the State of Illinois, hereby executes the following Articles of Amendment:

**PAID**

MAR 15 1971

ARTICLE FIRST: The name of the corporation is:

North Shore Gas Company

ARTICLE SECOND: The following amendment or amendments were adopted in the manner prescribed by "The Business Corporation Act" of the State of Illinois:

*John W. Lewis*  
Secretary of State

Article Five of the Articles of Incorporation of North Shore Gas Company is amended to read as follows:

"ARTICLE FIVE

"PARAGRAPH 1: The aggregate number of shares which the corporation is authorized to issue is 3,000,000, divided into one (1) class. The designation of each class, the number of shares of each class, and the par value, if any, of the shares of each class, or a statement that the shares of any class are without par value, are as follows:

Class	Series (If any)	Number of Shares	Par value per share or statement that shares are without par value
Common	-	3,000,000	Without par value "



Not Applicable

(Disregard separation into classes if class voting does not apply to the amendment voted on.)

ARTICLE THIRD: The number of shares of the corporation outstanding at the time of the adoption of said amendment or amendments was 1,727,134; and the number of shares of each class entitled to vote as a class on the adoption of said amendment or amendments, and the designation of each such class were as follows:

Class	Number of Shares
-------	------------------

(Disregard separation into classes if class voting does not apply to the amendment voted on.)

ARTICLE FOURTH: The number of shares voted for said amendment or amendments was 1,727,134; and the number of shares voted against said amendment or amendments was none

The number of shares of each class entitled to vote as a class voted for and against said amendment or amendments, respectively, was:

Class	Number of Shares Voted For	Against
-------	----------------------------	---------

(Disregard these items unless the amendment restates the articles of incorporation.)

Item 1. On the date of the adoption of this amendment, restating the articles of incorporation, the corporation had \_\_\_\_\_ shares issued, itemized as follows:

Class	Series (If Any)	Number of Shares	Par value per share or statement that shares are without par value
-------	-----------------	------------------	--

Not Applicable

Item 2. On the date of the adoption of this amendment restating the articles of incorporation, the corporation had a stated capital of \$ \_\_\_\_\_ and a paid-in surplus of \$ \_\_\_\_\_ or a total of \$ \_\_\_\_\_

(Disregard this Article where this amendment contains no such provisions.)

ARTICLE FIFTH: The manner in which the exchange, reclassification, or cancellation of issued shares, or a reduction of the number of authorized shares of any class below the number of issued shares of that class, provided for in, or effected by, this amendment, is as follows:

Not Applicable

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

ARTICLE SIXTH: Paragraph 1: The manner in which said amendment or amendments effect a change in the amount of stated capital or the amount of paid-in surplus, or both, is as follows:

Not Applicable

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

Paragraph 2: The amounts of stated capital and of paid-in surplus as changed by this amendment are as follows:

	Before Amendment	After Amendment
Stated capital.....\$		\$
Paid-in surplus.....\$		\$

Not Applicable

15

IN WITNESS WHEREOF, the undersigned corporation has caused these Articles of Amendment to be executed in its name by its Vice President, and its corporate seal to be hereto affixed, attested by its Assistant Secretary, this 10th day of March, 1971.

North Shore Gas Company  
(Exact Corporate Name)

PLACE  
HERE  
(CORPORATE SEAL)

ATTEST:

E. Q. J. Mary  
is Assistant Secretary

By Joseph P. Thomas  
Vice President

STATE OF Illinois  
COUNTY OF Cook }

I, Margot G. Hodel, Notary Public, do hereby certify that on the 10th day of March, 1971, Joseph P. Thomas personally appeared before me and, being first duly sworn by me, acknowledged that he signed the foregoing document in the capacity therein set forth and declared that the statements therein contained are true.

IN WITNESS WHEREOF, I have hereunto set my hand and seal the day and year before written.

PLACE  
HERE  
(NOTARIAL SEAL)

Margot G. Hodel  
Notary Public

Box 6344 File 1-3

ARTICLES OF AMENDMENT  
to the  
ARTICLES OF INCORPORATION  
of

North Shore Gas Company

MAR 13 1971  
Joseph P. Thomas  
Secretary in State

FILE IN DUPLICATE

Filing Fee \$25.00

Filing Fee for Re-Stated Articles \$100.00



**To all to whom these Presents Shall Come, Greeting:**

**Whereas**, *Articles of amendment to the Articles of Incorporation*  
*duly signed and verified of* \_\_\_\_\_

**NORTH SHORE GAS COMPANY**

*have been filed in the Office of the Secretary of State, on the* \_\_\_\_\_ **23rd**  
*day of* **April** *A. D. 19* **75**, *as provided by "THE BUSINESS*  
*CORPORATION ACT" of Illinois, in force July 13, A. D. 1933.*

*Now Therefore, I, MICHAEL J. HOWLETT, Secretary of State of the State of Illinois,*  
*by virtue of the powers vested in me by law, do hereby, issue this certificate of*  
*amendment, and attach thereto a copy of the Articles of Amendment to*  
*the Articles of Incorporation of the aforesaid corporation.*

**In Testimony Whereof**, *I thereto set my hand and cause to*  
*be affixed the Great Seal of the State of Illinois.*

*Done at the City of Springfield this* \_\_\_\_\_ **23rd**  
*day of* **April** *A. D. 19* **75** *and*  
*of the Independence of the United States*  
*the one hundred and* \_\_\_\_\_ **99th**

\_\_\_\_\_  
SECRETARY OF STATE.

(Do not write in this space)

Date Paid

License Fee

Franchise Tax

Filing Fee

Clerk

\$

\$

\$

\$

(File in Duplicate)

# ARTICLES OF AMENDMENT TO THE ARTICLES OF INCORPORATION OF

## NORTH SHORE GAS COMPANY

(Exact Corporate Name)

To MICHAEL J. HOWLETT

Secretary of State  
Springfield, Illinois

The undersigned corporation, for the purpose of amending its Articles of Incorporation and pursuant to the provisions of Section 55 of "The Business Corporation Act" of the State of Illinois, hereby executes the following Articles of Amendment:

ARTICLE FIRST: The name of the corporation is: North Shore Gas Company

ARTICLE SECOND: The following amendment or amendments were adopted in the manner prescribed by "The Business Corporation Act" of the State of Illinois: Article Five of the Articles of Incorporation of North Shore Gas Company is amended to read as follows:

### ARTICLE FIVE

Paragraph 1: The aggregate number of shares which the corporation is authorized to issue is 4,000,000, divided into one (1) class. The designation of each class, the number of shares of each class, and the par value, if any, of the shares of each class, or a statement that the shares of any class are without par value, are as follows:

Class	Series (if any)	Number of Shares	Par value per share or statement that shares are without par value
Common	-	4,000,000	Without par value

APR 24 1975

Michael J. Howlett

(Disregard separation into classes if class voting does not apply to the amendment voted on.)

ARTICLE THIRD: The number of shares of the corporation outstanding at the time of the adoption of said amendment or amendments was 2,652,134 common shares; and the number of shares of each class entitled to vote as a class on the adoption of said amendment or amendments, and the designation of each such class were as follows:

Class	Number of Shares
-------	------------------

not applicable

(Disregard separation into classes if class voting does not apply to the amendment voted on.)

ARTICLE FOURTH: The number of shares voted for said amendment or amendments was 2,652,134; and the number of shares voted against said amendment or amendments was none. The number of shares of each class entitled to vote as a class voted for and against said amendment or amendments, respectively, was:

Class	Number of Shares Voted	
	For	Against

not applicable

(Disregard these items unless the amendment restates the articles of incorporation.)

Item 1. On the date of the adoption of this amendment, restating the articles of incorporation, the corporation had \_\_\_\_\_ shares issued, itemized as follows:

Class	Series (If Any)	Number of Shares	Par value per share or statement that shares are without par value
-------	--------------------	---------------------	---

not applicable

Item 2. On the date of the adoption of this amendment restating the articles of incorporation, the corporation had a stated capital of \$\_\_\_\_\_ and a paid-in surplus of \$\_\_\_\_\_ or a total of \$\_\_\_\_\_.

Certificate \_\_\_\_\_



To all to whom these Presents Shall Come, Greeting:

Whereas, Articles of amendment to the Articles of Incorporation duly signed and verified of \_\_\_\_\_  
NORTH SHORE GAS COMPANY

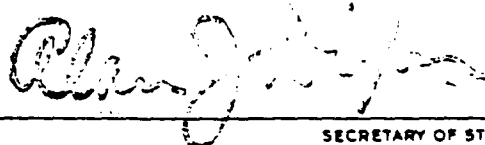
have been filed in the Office of the Secretary of State, on the \_\_\_\_\_ 4th  
day of February A. D. 19<sup>th</sup>, as provided by "THE BUSINESS  
CORPORATION ACT" of Illinois, in force July 13, A. D. 1933.

Now Therefore, I, <sup>Alan J. Dixon</sup> ~~MICHAEL THOMAS~~ ET, Secretary of State of the State of Illinois  
by virtue of the powers vested in me by law, do hereby issue this certificate of  
amendment, and attach thereto a copy of the Articles of Amendment to  
the Articles of Incorporation of the aforesaid corporation.

In Testimony Whereof, I thereto set my hand and cause to  
be affixed the Great Seal of the State of Illinois.

Done at the City of Springfield this \_\_\_\_\_ 4th  
day of February A. D. 19<sup>th</sup> and  
of the Independence of the United States  
the two hundred and \_\_\_\_\_ 1st

(SEAL)



SECRETARY OF STATE

(Disregard this Article where this amendment contains no such provisions.)

ARTICLE FIFTH: The manner in which the exchange, reclassification, or cancellation of issued shares, or a reduction of the number of authorized shares of any class below the number of issued shares of that class, provided for in, or effected by, this amendment, is as follows:

not applicable

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

ARTICLE SIXTH: Paragraph 1: The manner in which said amendment or amendments effect a change in the amount of stated capital or the amount of paid-in surplus, or both, is as follows:

not applicable

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

Paragraph 2: The amounts of stated capital and of paid-in surplus as changed by this amendment are as follows:

	Before Amendment	After Amendment
Stated capital.....\$		\$
Paid-in surplus.....\$		\$

not applicable



Box

File

ARTICLES OF AMENDMENT  
to the  
ARTICLES OF INCORPORATION  
of

FILED

APR 23 1975

Michael J. Howlett  
Secretary of State

FILE IN DUPLICATE

Filing Fee \$25.00

Filing Fee for Re-Stated Articles \$100.00

IN WITNESS WHEREOF, the undersigned corporation has caused these Articles of Amendment to be executed in its name by its Vice President, and its corporate seal to be hereto affixed, attested by its Assistant Secretary, this 18th day of April, 19 75.

Place  
(CORPORATE SEAL)  
Here

North Shore Gas Company  
(Exact Corporate Name)  
By William C. Terpstra  
Its Vice President

ATTEST:

Its Asst. Secretary

*[Signature]*

STATE OF Illinois  
COUNTY OF COOK } ss.

I, Marilyn J. Yates, a Notary Public, do hereby certify that on the 18th day of April, 19 75, William C. Terpstra personally appeared before me and, being first duly sworn by me, acknowledged that he signed the foregoing document in the capacity therein set forth and declared that the statements therein contained are true.

IN WITNESS WHEREOF, I have hereunto set my hand and seal the day and year before written.

Place  
(NOTARIAL SEAL)  
Here

*[Signature]*  
Notary Public

(File in Duplicate)

(Do not write in this space)	
Date Paid	/ /
License Fee	\$
Franchise Tax	\$
Filing Fee	\$
Clerk	

**ARTICLES OF AMENDMENT  
TO THE  
ARTICLES OF INCORPORATION  
OF**

**NORTH SHORE GAS COMPANY**  
(Exact Corporate Name)

TO ALAN J. DIXON  
Secretary of State  
Springfield, Illinois

The undersigned corporation, for the purpose of amending its Articles of Incorporation and pursuant to the provisions of Section 55 of "The Business Corporation Act" of the State of Illinois, hereby executes the following Articles of Amendment:

ARTICLE FIRST: The name of the corporation is:

**NORTH SHORE GAS COMPANY**

ARTICLE SECOND: The following amendment or amendments were adopted in the manner prescribed by "The Business Corporation Act" of the State of Illinois:

**PAID**

**FEB 4 1977**

**ALAN J. DIXON**  
Secretary of State

**RESOLVED:** That **ARTICLE FIVE** of the Articles of Incorporation of North Shore Gas Company (the "Company") be amended so as to read in its entirety as follows:

**ARTICLE FIVE**

Paragraph 1: The aggregate number of shares which the Company is authorized to issue is 5,250,000 divided into two classes. The designation of each class, the number of shares of each class, and the par value, if any, of the shares of each class, or a statement that the shares of any class are without par value, are as follows:

<u>Class</u>	<u>Series (If any)</u>	<u>Number of Shares</u>	<u>Par value per share or statement that shares are without par value</u>
\$100 Cumulative Preferred	See Paragraph 2-I(a)	250,000	\$100.00
Common	None	5,000,000	without par value

Paragraph 2: The preferences, qualifications, limitations, restrictions and the special or relative rights in respect of the shares of each class are:

#### I. \$100 CUMULATIVE PREFERRED STOCK

(a) *Issue of \$100 Cumulative Preferred Stock in Series.* Authority is hereby expressly vested in the Board of Directors to divide, and to provide for the issue from time to time of the \$100 Cumulative Preferred Stock in series, and to fix and determine as to each such series:

- (1) the designation of, and the number of shares to be issuable in, such series;
- (2) the dividend rate per annum for the shares of such series, expressed either as a dollar amount per share or as a percentage of the par value thereof, and the time of payment of such dividends;
- (3) the price or prices at which, and the terms and conditions on which, such shares may be redeemed;
- (4) the amount payable upon each of such shares in the event of voluntary dissolution, liquidation or winding up of the Company;
- (5) the amount payable upon each of such shares in the event of involuntary dissolution, liquidation or winding up of the Company;
- (6) sinking fund provisions, if any, for the redemption or purchase of such shares (the term "sinking fund", as used herein, including any analogous fund, however designated);
- (7) if such shares are to be issued with the privilege of conversion into shares of the Common Stock, the terms and conditions on which such shares may be so converted; and
- (8) other special rights and privileges of shares of such series as shall not be inconsistent with the provisions hereof.

In all other respects shares of the \$100 Cumulative Preferred Stock of all series shall be identical.

So long as any shares of any series of the \$100 Cumulative Preferred Stock shall be outstanding, the resolution of the Board of Directors establishing such series shall not be amended or revoked so as adversely to affect any of the preferences or other rights of the holders of the shares of such series, without the affirmative vote or the written consent of the holders of at least two-thirds of the shares of such series outstanding at the time or as of a record date fixed by the Board of Directors, but such resolution may be so amended or revoked with such vote or consent.

(b) *Priority.* The \$100 Cumulative Preferred Stock shall be prior and senior to the Common Stock as to the payment of dividends and as to the distribution of assets upon dissolution, liquidation or winding up of the Company.

(c) *Dividends.* Holders of the \$100 Cumulative Preferred Stock of each series shall be entitled to receive cash dividends, out of funds legally available therefor, when and as declared by the Board of Directors, at such rate per annum and payable on such dates as shall have been fixed by the Board of Directors for the shares of such series. Dividends on the \$100 Cumulative Preferred Stock of each series

shall be cumulative with respect to each share from the date of issue thereof. Accumulations of dividends shall not bear interest. Whenever there shall be paid on the shares of any series of the \$100 Cumulative Preferred Stock the full amount or any part of the dividends payable thereon, there shall also be paid at the same time on the shares of each other series of \$100 Cumulative Preferred Stock, if any, then outstanding the full amount or a like proportionate part, as the case may be, of the dividends payable thereon.

No funds shall be paid into or set aside for any sinking fund created for any series of the \$100 Cumulative Preferred Stock or for any stock of any class ranking on a parity with or junior to the \$100 Cumulative Preferred Stock with respect to the payment of dividends or the distribution of assets, unless all dividends on the \$100 Cumulative Preferred Stock for all past dividend periods, and for the current dividend period, shall have been paid in full or shall have been declared and funds sufficient for such payment set aside by the Company, separate and apart from its other funds.

No dividend shall be paid or other distribution made on any stock of any class ranking on a parity with or junior to the \$100 Cumulative Preferred Stock with respect to the payment of dividends or the distribution of assets, other than a dividend or distribution solely of shares of such stock, and no such stock shall be redeemed, purchased or otherwise acquired by the Company for a consideration, unless (1) all dividends on the \$100 Cumulative Preferred Stock for all past dividend periods, and for the current dividend period, shall have been paid in full or shall have been declared and funds sufficient for such payment set aside by the Company, separate and apart from its other funds, and (2) all funds then and theretofore required to be paid into or set aside for any sinking fund or funds created for all series of the \$100 Cumulative Preferred Stock shall have been so paid or set aside.

(d) *Redemption of \$100 Cumulative Preferred Stock.* Subject to the limitations stated in subdivisions (c) and (e) hereof and except as may be otherwise provided by the Board of Directors in respect of the shares of a particular series, shares of any one or more series of the \$100 Cumulative Preferred Stock may be called for redemption and redeemed, at the option of the Company, in whole at any time or in part from time to time, upon the notice hereinafter provided for, by the payment therefor in cash of the then applicable optional redemption price or prices fixed by the Board of Directors for the shares which are to be redeemed.

If at any time less than all shares of any series of the \$100 Cumulative Preferred Stock shall be called for redemption, the shares so called shall be selected by lot in such manner, or pro rata, all as may be determined by the Board of Directors.

Notice of any proposed redemption shall be given by the Company by first class mail, postage prepaid, or caused by the Company to be so given, not more than 60 nor less than 30 days prior to the redemption date, to the holders of record of the shares to be redeemed at their respective addresses then appearing, on the records of the Company.

At any time before the redemption date the Company may deposit in trust the funds necessary for such redemption with a bank or trust company, to be designated in the notice of such redemption, doing business in the City of Chicago, State of Illinois, or in the Borough of Manhattan, The City of New York, State of New York, and having capital, surplus and undivided profits aggregating at least \$5,000,000. In the event such deposit is made so that the deposited funds shall be forthwith available to the holders of the shares to be redeemed upon surrender of the certificates evidencing such shares, then, upon the giving of the notice of such redemption, as hereinabove provided, or upon the earlier delivery to such bank or trust company of irrevocable authorization and direction so to give such notice, all shares with respect to the redemption of which such deposit shall have been made and the giving of such notice effected or authorization therefor given shall, whether or not the certificates for such shares shall have been surrendered for cancellation, be deemed to be no longer outstanding for any purpose and all rights with respect to such shares shall thereupon cease and terminate, except only the right of the holders of the certificates for such shares (1) to receive, out of the funds so deposited in trust, from and after the time of such deposit, the amount payable upon the redemption thereof, without interest, or (2) to exercise any privilege of conversion which shall not theretofore have terminated.

Any funds so deposited which shall not be required for the payment of the redemption price of such shares by reason of the exercise of any right of conversion subsequent to the date of such deposit shall be paid over to the Company forthwith. At the expiration of six years after the redemption date, any such funds then remaining on deposit with such bank or trust company shall be paid over to the Company, free of trust, and thereafter the holders of the certificates for such shares shall have no claims against such bank or trust company, but only claims as unsecured creditors against the Company for amounts equal to their pro rata portions of the funds so paid over, without interest. Any interest on or other accretions to funds deposited with such bank or trust company shall belong to the Company.

The provisions of this subdivision (d) with respect to the method and effect of redemption shall be applicable to the redemption of shares pursuant to any sinking fund created for any series of the \$100 Cumulative Preferred Stock as well as to the optional redemption of shares, except to the extent, if any, that the terms of such sinking fund, as fixed and determined by the Board of Directors, shall expressly otherwise provide.

(e) *Limitations on Redemption and Purchase of \$100 Cumulative Preferred Stock.* If and so long as the Company shall be in default in the payment of any dividend on shares of any series of the \$100 Cumulative Preferred Stock, or shall be in default in the payment of funds into or the setting aside of funds for any sinking fund created for any series of the \$100 Cumulative Preferred Stock, the Company shall not (other than by the use of unapplied funds, if any, paid into or set aside for a sinking fund or funds prior to such default) redeem, purchase or otherwise acquire for a consideration any shares of the \$100 Cumulative Preferred Stock unless (i) all shares thereof are redeemed or (ii) such purchase or acquisition is made pursuant to an offer to purchase at the respective redemption prices made on a comparable basis to the holders of all shares of the \$100 Cumulative Preferred Stock then outstanding.

(f) *Status of \$100 Cumulative Preferred Stock Redeemed, Purchased or Otherwise Reacquired.* All shares of the \$100 Cumulative Preferred Stock of any series which shall have been redeemed, purchased or otherwise reacquired by the Company shall be cancelled and shall not be issued as shares of such series.

(g) *Liquidation Preference.* In the event of dissolution, liquidation or winding up of the Company, whether voluntary or involuntary, holders of the \$100 Cumulative Preferred Stock of each series shall be entitled to receive out of the assets of the Company, before any payment or distribution shall be made to the holders of Common Stock or of any other stock of the Company ranking junior to the \$100 Cumulative Preferred Stock with respect to the payment of dividends or the distribution of assets, such amount per share as shall have been fixed by the Board of Directors as the dissolution, liquidation or winding up price, as the case may be, for the shares of such series. If upon any such dissolution, liquidation or winding up, the assets of the Company available for payment to stockholders are not sufficient to make payment in full to holders of the \$100 Cumulative Preferred Stock, payment shall be made to such holders ratably in accordance with the numbers of shares held by them respectively, and, in case there shall then be outstanding more than one series of the \$100 Cumulative Preferred Stock, ratably in accordance with the respective distributive amounts to which such holders shall be entitled.

Neither a consolidation or merger of the Company with or into any other corporation, nor a merger of any other corporation into the Company, nor the redemption or purchase by the Company of all or a part of the outstanding shares of any class or classes of its stock, nor a sale or transfer of the property and business of the Company, as or substantially as an entirety, shall be considered a dissolution, liquidation or winding up of the Company within the meaning of the foregoing provisions.

(h) *Restriction on Certain Corporate Action.* (1) So long as any shares of the \$100 Cumulative Preferred Stock shall be outstanding,

(A) the Company shall not, without the affirmative vote or the written consent of the holders of at least two-thirds of the shares of the \$100 Cumulative Preferred Stock outstanding at the time or as of a record date fixed by the Board of Directors, create or authorize any stock of any class ranking prior to or on a parity with the \$100 Cumulative Preferred Stock with respect to the payment of dividends or the distribution of assets; and

(B) the Company shall not amend the Articles of Incorporation of the Company so as adversely to affect any of the preferences or other rights of the holders of the \$100 Cumulative Preferred Stock without (i) the affirmative vote or the written consent of the holders of at least two-thirds of the shares of the \$100 Cumulative Preferred Stock outstanding at the time or as of a record date fixed by the Board of Directors and (ii) the affirmative vote or the written consent of the holders of at least two-thirds of the shares of each series of the \$100 Cumulative Preferred Stock so adversely affected outstanding at the time or as of a record date fixed by the Board of Directors.

(2) So long as any shares of the \$100 Cumulative Preferred Stock shall be outstanding, the Company shall not, without the affirmative vote or the written consent of the holders of a majority of the shares of the \$100 Cumulative Preferred Stock outstanding at the time or as of a record date fixed by the Board of Directors, consolidate with or merge into any other corporation, under applicable statutory procedure, or make any sale or transfer of the property and business of the Company as or substantially as an entirety; provided, however, that this restriction shall not apply to a consolidation of the Company with or its merger into or the sale or transfer of the property and business of the Company as or substantially as an entirety to (i) any corporation which as of February 15, 1977 owned directly, or indirectly through one or more other corporations, 50% or more of the voting securities of the Company, (ii) any corporation, 50% or more of the voting securities of which were so owned by the Company as of February 15, 1977, or (iii) any corporation, when such consolidation, merger, sale or transfer shall be required by order or regulation of any commission or other governmental agency having jurisdiction in the premises. The term "sale or transfer", as used in this subpart (h), includes a lease or exchange but does not include a mortgage or pledge.

(i) *Preemptive Rights.* Holders of the \$100 Cumulative Preferred Stock shall not have any preemptive rights.

## II. COMMON STOCK

(a) *Dividends.* Subject to the preferential rights of the holders of the \$100 Cumulative Preferred Stock with respect to the payment of dividends and sinking fund payments, as set forth in subdivision (c) of Division I, holders of the Common Stock shall be entitled to receive dividends, out of funds legally available therefor, when and as declared by the Board of Directors.

(b) *Liquidation Preferences.* In the event of dissolution, liquidation or winding up of the Company, whether voluntary or involuntary, holders of the Common Stock shall be entitled to receive, ratably in accordance with the numbers of shares held by them respectively, the assets of the Company, available for payment to shareholders, remaining after payment in full shall have been made to holders of the \$100 Cumulative Preferred Stock in accordance with the provisions of subdivision (g) of Division I.

Neither a consolidation or merger of the Company with or into any other corporation, nor a merger of any other corporation into the Company, nor the redemption or purchase by the Company of all or a part of the outstanding shares of any class or classes of its stock, nor a sale or transfer of the property and business of the Company, as or substantially as an entirety, shall be considered a dissolution, liquidation or winding up of the Company within the meaning of the foregoing provisions.

(c) *Preemptive Rights.* Holders of the Common Stock shall not have any preemptive rights.

Disregard separation into classes  
f class voting does not apply to  
he amendment voted on.)

ARTICLE THIRD: The number of shares of the corporation outstanding at the time of the adoption of said amendment or amendments was 3,150,887 common shares; and the number of shares of each class entitled to vote as a class on the adoption of said amendment or amendments, and the designation of each such class were as follows:

Class

Number of Shares

Inapplicable

(Disregard separation into classes if class voting does not apply to the amendment voted on.)

**ARTICLE FOURTH:** The number of shares voted for said amendment or amendments was 3,150,887; and the number of shares voted against said amendment or amendments was 00. The number of shares of each class entitled to vote as a class voted for and against said amendment or amendments, respectively, was:

Class	Number of Shares Voted	
	For	Against
	Inapplicable	

(Disregard these items unless the amendment restates the articles of incorporation.)

**Item 1.** On the date of the adoption of this amendment, restating the articles of incorporation, the corporation had \_\_\_\_\_ shares issued, itemized as follows:

Class	Series (If Any)	Number of Shares	Par value per share or statement that shares are without par value
Inapplicable			

**Item 2.** On the date of the adoption of this amendment restating the articles of incorporation, the corporation had a stated capital of \$\_\_\_\_\_ and a paid-in surplus of \$\_\_\_\_\_ or a total of \$\_\_\_\_\_

Inapplicable

(Disregard this Article where this amendment contains no such provisions.)

**ARTICLE FIFTH:** The manner in which the exchange, reclassification, or cancellation of issued shares, or a reduction of the number of authorized shares of any class below the number of issued shares of that class, provided for in, or effected by, this amendment, is as follows:

Inapplicable

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

**ARTICLE SIXTH: Paragraph 1:** The manner in which said amendment or amendments effect a change in the amount of stated capital or the amount of paid-in surplus, or both, is as follows:

Inapplicable

(Disregard this Paragraph where amendment does not affect stated capital or paid-in surplus.)

**Paragraph 2:** The amounts of stated capital and of paid-in surplus as changed by this amendment are as follows:

	Before Amendment	After Amendment
Stated capital .....	\$	\$
Paid-in surplus .....	\$	\$
Inapplicable		

IN WITNESS WHEREOF, the undersigned corporation has caused these Articles of Amendment to be executed in its name by its \_\_\_\_\_ President, and its corporate seal to be hereto affixed, attested by its \_\_\_\_\_ Assistant Secretary, this 3rd day of February, 19 77

Place  
(CORPORATE SEAL)  
Here

North Shore Gas Company  
By \_\_\_\_\_ (Exact Corporate Name)  
is \_\_\_\_\_ President

ATTEST:

is Assistant Secretary

STATE OF ILLINOIS  
COUNTY OF COOK } ss.

I, \_\_\_\_\_ Rita Thomas \_\_\_\_\_ on the 3rd day of February 19 77 \_\_\_\_\_ a Notary Public, do hereby certify that appeared before me and, being first duly sworn by me, acknowledged that he signed the foregoing document in the capacity therein set forth and declared that the statements therein contained are true. \_\_\_\_\_ George L. Morrow \_\_\_\_\_ personally

IN WITNESS WHEREOF, I have hereunto set my hand and seal the day and year before written.

Place  
(NOTARIAL SEAL)  
Here

Notary Public  
My Commission Expires  
June 30, 1980

Box 549 File 143-1

ARTICLES OF AMENDMENT  
to the  
ARTICLES OF INCORPORATION  
of  
NORTH SHORE GAS COMPANY

FILED

FEB 4 1977

*George L. Morrow*  
Notary Public

FILE IN DUPLICATE

Filing Fee \$25.00

Filing Fee for Re-Stated Articles \$100.00



File No. D4349-113-1

Date 4-13-82

File in duplicate

Filing Fee \$ 5.00

Please read instructions on back  
before attempting to execute

Clerk AS

**CERTIFICATE OF CHANGE OF REGISTERED AGENT AND REGISTERED OFFICE BY  
A FOREIGN OR DOMESTIC CORPORATION OF ILLINOIS**

To

Secretary of State  
Springfield, Illinois

The undersigned corporation, organized and existing under the laws of the State of Illinois for the purpose of changing its registered agent or its registered office, or both, in Illinois as provided by "The Business Corporation Act", of Illinois represents that:

1. The name of the corporation is North Shore Gas Company

2. The address, including street and number, if any, of its present registered office (before change) is Room 213,  
122 South Michigan Avenue, Chicago, Illinois 60603

3. Its registered office (including street and number if any change in the registered office is to be made) is hereby changed to  
Room 1609, 122 S. Michigan Avenue -Street, Chicago  
IL ( 60603 ) County of Cook  
(Zip Code)

4. The name of its present registered agent (before change) is Donald G. Holm

5. The name of the new registered agent is Same

6. The address of its registered office and the address of the business office of its registered agent, ~~as changed~~, will be identical.

7. The manner of authorization of such change(s) was:

- a. ☐ By resolution duly authorized by the board of directors;  
b. ☒ By action of its registered agent.

## SIGNATURES

(Sign below where the above change(s) were authorized  
' resolution of the board of directors.)

Under penalty of perjury and as an authorized officer of  
the corporation, I declare that this document has been  
examined by me and is, to the best of my knowledge  
and belief, true, correct, and complete.

IN WITNESS WHEREOF, I have hereunto subscribed  
my name and affixed the seal of said corporation, on  
this \_\_\_\_\_ day of \_\_\_\_\_ 19 \_\_\_\_\_.

By \_\_\_\_\_  
(Pres. or Vice-Pres.) (Title)

seal

Attest \_\_\_\_\_  
(Sec. or Assist. Sec.) (Title)

(Sign below where the above change of address was  
authorized by action of the registered agent.)

Under penalty of perjury and as the authorized registered  
agent of the corporation, I declare that this document  
has been examined by me and is, to the best of my  
knowledge and belief, true, correct, and complete.

IN WITNESS WHEREOF, I have hereunto subscribed  
my name on this 29th day of March  
19 82.

By   
Registered Agent

## INSTRUCTIONS

1. The registered office may, but need not be the same as the principal office of the corporation. However, the registered office and the office address of the agent must be the same.
2. The registered office must be in Illinois and must be a street or road address, not a post office box number.
3. A registered agent may change the address of the registered office of the corporation, for which he is registered agent, to another address in this State.
4. If the registered office is changed from one county to another, then the corporation must file with the recorder of deeds of the new county a certified copy of the articles of incorporation and a certified copy of the statement of the change of registered office. Such certified copies may be obtained only from the Secretary of State.
5. A corporation cannot act as its own registered agent.

Form PCA (2, 12a, 110, 110a)

File No.

4349-143-1

CERTIFICATE OF CHANGE OF  
REGISTERED AGENT AND/OR  
OFFICE OF A FOREIGN OR  
DOMESTIC CORPORATION

Secretary of State  
Corporation Department  
Springfield, Illinois 62756  
Telephone: (217) 782-3647

FILED  
Filing Fee \$5.00

APR 13 1982

PAIL

APR 19 1982

C-135.2

Exhibit Z

**BY-LAWS**  
**OF**  
**NORTH SHORE GAS COMPANY**

**AMENDED JULY 5, 1989**

NORTH SHORE GAS COMPANY

BY-LAWS

ARTICLE I	-	OFFICES
ARTICLE II	-	MEETINGS OF SHAREHOLDERS
ARTICLE III	-	DIRECTORS AND COMMITTEES
ARTICLE IV	-	OFFICERS
ARTICLE V	-	INDEMNIFICATION OF DIRECTORS, OFFICERS AND EMPLOYES
ARTICLE VI	-	CERTIFICATES OF STOCK AND THEIR TRANSFER
ARTICLE VII	-	MISCELLANEOUS (CONTRACTS)
ARTICLE VIII	-	AMENDMENT OR REPEAL OF BY-LAWS

# NORTH SHORE GAS COMPANY

## INDEX

### PAGE

#### A

Amendment of By-Laws.....	15
Appointment of Officers.....	7
Assistant Controller, Duties of.....	11
Assistant General Counsel, Duties of.....	11
Assistant Secretary, Duties of.....	11
Assistant Treasurer, Duties of.....	11
Assistant Vice President, Duties of.....	9

#### B

Board of Directors.....	4
-------------------------	---

#### C

Certificates of Stock and Their Transfer.....	12
Chairman of the Board, Duties of.....	8
Committees.....	6
Controller, Duties of.....	10
Contracts, Execution of.....	14

#### D

Directors and Committees.....	4
-------------------------------	---

#### E

Election of Directors.....	4
Election of Officers.....	7

#### F

Fees and Compensation of Directors.....	6
---	---

#### G

General Counsel, Duties of.....	10
---------------------------------	----

# NORTH SHORE GAS COMPANY

	PAGE
I	
Indemnification of Directors, Officers and Employees .....	11
M	
Meetings	
Directors.....	4
Action Without Meeting.....	6
Shareholders.....	1
N	
Notice of Meetings	
Directors.....	4
Shareholders.....	2
O	
Officers	
Appointed.....	7
Elected.....	7
Offices, Two or More Held By One Person.....	7
P	
President, Duties of.....	9
Presiding Officer	
Board Meetings.....	6
Shareholders Meetings.....	4
Proxies.....	3
Q	
Quorum	
Board.....	5
Shareholders.....	2
S	
Secretary, Duties of.....	9
Signatures to Checks, Drafts, etc.....	14
Stock, Certificates of and their Transfer.....	12

NORTH SHORE GAS COMPANY

PAGE

T

Treasurer, Duties of.....	10
---------------------------	----

V

Vice President, Duties of.....	9
Voting	
Shareholders.....	3
Stock Owned by Company.....	15

BY-LAWS  
OF  
NORTH SHORE GAS COMPANY

ARTICLE I

Offices

SECTION 1.1. Principal Office. The principal office of the Company shall be in the City of Chicago, County of Cook and State of Illinois.

SECTION 1.2. Other Offices. The Company may also have offices at such other places both within and without the State of Illinois as the Board of Directors may from time to time determine or the business of the Company may require.

ARTICLE II

Meetings of Shareholders

SECTION 2.1. Annual Meeting. The annual meeting of the shareholders shall be held on the last Thursday of the month of March in each year, if not a legal holiday, or, if a legal holiday, then on the next preceding business day, for the purpose of electing directors and for the transaction of such other business as may come before the meeting. If the election of directors shall not be held on the day herein designated for the annual meeting, or at any adjournment thereof, the Board of Directors shall cause such election to be held at a special meeting of the shareholders as soon thereafter as convenient.



SECTION 2.2. Special Meetings. Except as otherwise prescribed by statute, special meetings of the shareholders for any purpose or purposes, may be called by the Chairman of the Board, the President, a majority of the Board of Directors or shareholders owning capital stock of the Company having not less than 20% of the total voting power. Such request shall state the purpose or purposes of the proposed meeting.

SECTION 2.3. Place of Meetings. Each meeting of the shareholders for the election of directors shall be held at the principal office of the Company in the City of Chicago, Illinois, unless the Board of Directors shall by resolution designate another place as the place of such meeting. Meetings of shareholders for any other purpose may be held at such place, and at such time as shall be determined by the Chairman of the Board, or the President, or in their absence, by the Secretary, and stated in the notice of the meeting or in a duly executed waiver of notice thereof.

SECTION 2.4. Notice of Meetings. Written or printed notice stating the place, date and hour of each annual or special meeting of the shareholders, and, in the case of a special meeting, the purpose or purposes for which the meeting is called, shall be given not less than 10 or more than 60 days before the date of the meeting, except as otherwise provided by statute. Notice of any meeting of the shareholders may be waived by any shareholder.

SECTION 2.5. Quorum. The holders of a majority of the shares issued and outstanding and entitled to vote thereat, present in person or represented by proxy, shall be requisite for, and shall

constitute, a quorum at all meetings of the shareholders of the Company for the transaction of business, except as otherwise provided by statute or these by-laws. If a quorum shall not be present or represented at any meeting of the shareholders, the shareholders entitled to vote thereat, present in person or represented by proxy, shall have power to adjourn the meeting from time to time, without notice other than announcement at the meeting if the adjournment is for thirty days or less or unless after the adjournment a new record date is fixed, until a quorum shall be present or represented. At such adjourned meeting, at which a quorum shall be present or represented, any business may be transacted which might have been transacted at the meeting as originally noticed.

**SECTION 2.6. Proxies.** At every meeting of the shareholders, each shareholder having the right to vote thereat shall be entitled to vote in person or by proxy. Such proxy shall be appointed by an instrument in writing subscribed by such shareholder and bearing a date not more than eleven months prior to such meeting, unless such proxy provides for a longer period, and shall be filed with the Secretary of the Company before, or at the time of, the meeting.

**SECTION 2.7. Voting.** At each meeting of the shareholders, each shareholder shall be entitled to one vote for each share of stock entitled to vote thereat which is registered in the name of such shareholder on the books of the Company. At all elections of directors of the Company, the holders of shares of stock of the Company shall be entitled to cumulative voting. When a quorum is

present at any meeting of the shareholders, the vote of the holders of a majority of the shares present in person or represented by proxy and entitled to vote at the meeting shall be sufficient for the transaction of any business, unless otherwise provided by statute or these by-laws.

SECTION 2.8. Presiding Officer. The presiding officer of any meeting of the shareholders shall be the Chairman of the Board or, in the case of the absence of the Chairman of the Board, the President.

### ARTICLE III

#### Directors and Committees

SECTION 3.1. Number and Election. The business and affairs of the Company shall be managed and controlled by a board of directors, six (6) in number, none of whom needs to be a shareholder. The directors shall be elected by the shareholders entitled to vote at the annual meeting of such shareholders and each director shall be elected to serve for a term of one (1) year and thereafter until his successor shall be elected and shall qualify. In the event of a vacancy on the Board by reason of death, resignation or otherwise, the vacancy may be filled by vote of the shareholders at the next annual meeting or at a special meeting called for such purpose.

SECTION 3.2. Regular Meetings. A regular meeting of the Board of Directors shall be held immediately, or as soon as practicable, after the annual meeting of the shareholders in each year for the purpose of electing officers and for the transaction of such other business as may be deemed necessary, and regular meetings of the Board shall be held at such date and time and at such place as

the Board of Directors may from time to time determine. Not less than two days' notice of all regular meetings of the Board, except the meeting to be held after the annual meeting of shareholders which shall be held without other notice than this by-law, shall be given to each director personally or by mail or telegram.

SECTION 3.3. Special Meetings. Special meetings of the Board may be called at any time by the Chairman of the Board, the President, or by any two directors, by causing the Secretary to mail to each director, not less than three days before the time of such meeting, a written notice stating the time and place of such meeting. Notice of any meeting of the Board may be waived by any director.

SECTION 3.4. Quorum. At each meeting of the Board of Directors, the presence of not less than a majority of the total number of directors specified in Section 3.1 hereof shall be necessary and sufficient to constitute a quorum for the transaction of business, and the act of a majority of the directors present at any meeting at which there is a quorum shall be the act of the Board of Directors, except as may be otherwise specifically provided by statute. If a quorum shall not be present at any meeting of directors, the directors present thereat may adjourn the meeting from time to time, without notice other than announcement at the meeting, until a quorum shall be present. In determining the presence of a quorum at a meeting of the directors or a committee thereof for the purpose of authorizing a contract or transaction between the Company and one or more of its directors, or between the Company and any other corporation, partnership, association, or other organization in

which one or more of the directors of this Company are directors or officers, or have a financial interest in such other organization, such interested directors may be counted in determining a quorum.

SECTION 3.5. Presiding Officer. The presiding officer of any meeting of the Board of Directors shall be the Chairman of the Board or, in his absence, the President or, in his absence, any other director elected chairman of the meeting by vote of a majority of the directors present at the meeting.

SECTION 3.6. Committees. The Board may appoint committees, standing or special, from time to time from among its own members or otherwise, and may confer such powers on such committees as the Board may determine and may revoke such powers and terminate the existence of such committees at its pleasure.

SECTION 3.7. Action Without Meeting. Any action required or permitted to be taken at any meeting of the Board of Directors, or any committee thereof, may be taken without a meeting if all members of the Board or of such committee, as the case may be, consent thereto in writing and such writing or writings are filed with the minutes of the proceedings of the Board or such committee.

SECTION 3.8. Fees and Compensation of Directors. Directors shall not receive any stated salary for their services as such; but, by resolution of the Board of Directors, reasonable fees, with or without expenses of attendance, may be allowed. Members of the Board shall be allowed their reasonable traveling expenses when actually engaged in the business of the Company, to be audited and allowed as in other cases of demands against the Company. Members of

standing or special committees may be allowed fees and expenses for attending committee meetings. Nothing herein contained shall be construed to preclude any director from serving the Company in any other capacity and receiving compensation therefor.

#### ARTICLE IV

##### Officers

SECTION 4.1. Election of Officers. There shall be elected by the Board of Directors in each year the following officers: a Chairman of the Board; a President; such number of Senior Vice Presidents, such number of Executive Vice Presidents, such number of Vice Presidents and such number of Assistant Vice Presidents as the Board at the time may decide upon; a Secretary; such number of Assistant Secretaries as the Board at the time may decide upon; a Treasurer; such number of Assistant Treasurers as the Board at the time may decide upon; and, if the Board may decide, a General Counsel; and such number of Assistant General Counsel as the Board at the time may decide upon. Any two or more offices may be held by one person, except that the offices of President and Secretary may not be held by the same person. All officers shall hold their respective offices during the pleasure of the Board.

SECTION 4.2. Appointment of Officers. The Board of Directors, the Chairman of the Board, or the President may from time to time appoint such other officers as may be deemed necessary, including one or more Vice Presidents, one or more Assistant Vice Presidents, one or more Assistant Secretaries, one or more Assistant Treasurers, a Controller, one or more Assistant Controllers, one or

more Assistant General Counsel, and such other agents, employees and attorneys-in-fact of the Company as may be deemed proper. Such officers, agents, employees and attorneys-in-fact shall have such authority, (which may include the authority to execute and deliver on behalf of the Company contracts and other instruments in writing of any nature), perform such duties and receive such compensation as the Board of Directors or, in the case of appointments made by the Chairman of the Board or the President, as the Chairman of the Board or the President, may from time to time prescribe and determine. The Board of Directors may from time to time authorize any officer to appoint and remove agents and employees, to prescribe their powers and duties and to fix their compensation therefor.

SECTION 4.3. Duties of Chairman of the Board. The Chairman of the Board shall be the chief executive officer of the Company and shall have control and direction of the management and affairs of the Company and may execute all contracts, deeds, assignments, certificates, bonds or other obligations for and on behalf of the Company, and sign certificates of stock and records of certificates required by law to be signed by the Chairman of the Board. When present, the Chairman of the Board shall preside at all meetings of the Board and of the shareholders. In the absence of the Chairman of the Board, due to his permanent disability, death, resignation or removal from office, the Vice Chairman of the Executive Committee shall promptly convene the Executive Committee to select a nominee for that office and submit said nominee's name to the Board of Directors for their consideration.

**SECTION 4.4. Duties of President.** Subject to the control and direction of the Chairman of the Board, and to the control of the Board, the President shall have general management of all the business of the Company, and he shall have such other powers and perform such other duties as may be prescribed for him by the Board or be delegated to him by the Chairman of the Board. He shall possess the same power as the Chairman of the Board to sign all certificates, contracts and other instruments of the Company. In case of the absence or disability of the President, or in case of his death, resignation or removal from office, the powers and duties of the President shall devolve upon the Chairman of the Board during absence or disability, or until the vacancy in the office of President shall be filled.

**SECTION 4.5. Duties of Vice President.** Each of the Senior Vice Presidents, Executive Vice Presidents, Vice Presidents and Assistant Vice Presidents shall have such powers and duties as may be prescribed for him by the Board, or be delegated to him by the Chairman of the Board or by the President. Each of such officers shall possess the same power as the President to sign all certificates, contracts and other instruments of the Company.

**SECTION 4.6. Duties of Secretary.** The Secretary shall have the custody and care of the corporate seal, records and minute books of the Company. He shall attend the meetings of the Board, and of the shareholders, and duly record and keep the minutes of the proceedings, and file and take charge of all papers and documents belonging to the general files of the Company, and shall have such



other powers and duties as are commonly incident to the office of Secretary or as may be prescribed for him by the Board, or be delegated to him by the Chairman of the Board or by the President.

SECTION 4.7. Duties of Treasurer. The Treasurer shall have charge of, and be responsible for, the collection, receipt, custody and disbursement of the funds of the Company, and shall deposit its funds in the name of the Company in such banks, trust companies or safety deposit vaults as the Board may direct. He shall have the custody of the stock record books and such other books and papers as in the practical business operations of the Company shall naturally belong in the office or custody of the Treasurer, or as shall be placed in his custody by the Board, the Chairman of the Board, the President, or any Vice President, and shall have such other powers and duties as are commonly incident to the office of Treasurer, or as may be prescribed for him by the Board, or be delegated to him by the Chairman of the Board or by the President.

SECTION 4.8. Duties of Controller. The Controller shall have control over all accounting records pertaining to moneys, properties, materials and supplies of the Company. He shall have charge of the bookkeeping and accounting records and functions, the related accounting information systems and reports and executive supervision of the system of internal accounting controls, and such other powers and duties as are commonly incident to the office of Controller or as may be prescribed by the Board, or be delegated to him by the Chairman of the Board or by the President.

SECTION 4.9. Duties of General Counsel. The General Counsel shall have full responsibility for all legal advice, counsel

and services for the Company and its subsidiaries including employment and retaining of attorneys and law firms as shall in his discretion be necessary or desirable and shall have such other powers and shall perform such other duties as from time to time may be assigned to him by the Board, the Chairman of the Board or the President.

SECTION 4.10. Duties of Assistant Secretary, Assistant Treasurer, Assistant Controller and Assistant General Counsel. The Assistant Secretary, Assistant Treasurer, Assistant Controller and Assistant General Counsel shall assist the Secretary, Treasurer, Controller and General Counsel, respectively, in the performance of the duties assigned to each and shall for such purpose have the same powers as his principal. He shall also have such other powers and duties as may be prescribed for him by the Board, or be delegated to him by the Chairman of the Board or by the President.

#### ARTICLE V

##### Indemnification of Directors, Officers and Employees

The Company shall indemnify any person who was or is a party, or is threatened to be made a party to any threatened, pending or completed action, suit or proceeding, whether civil, criminal, administrative or investigative by reason of the fact that he is or was a director, officer, employee or agent of the Company, or, at the request of the Company, is or was serving another corporation, partnership, joint venture, trust or other enterprise in any capacity, against expenses (including attorneys' fees), judgments, fines and amounts paid in settlement actually and reasonably incurred

by him in connection with such action, suit or proceeding, to the full extent permitted by the Business Corporation Act of the State of Illinois from time to time in effect. The indemnification provided by this Article V shall not be deemed exclusive of any other rights to which those seeking indemnification may be entitled under any statute, by-law, agreement, vote of shareholders or disinterested directors, or otherwise, both as to action in his official capacity and as to action in another capacity while holding such office, and shall continue as to a person who has ceased to be a director, officer, employe or agent, and shall inure to the benefit of the heirs, executors and administrators of such a person.

#### ARTICLE VI

##### Certificates of Stock and Their Transfer

SECTION 6.1. Certificates of Stock. The certificates of stock of the Company shall be in such form as may be determined by the Board of Directors, shall be numbered and shall be entered in the books of the Company as they are issued. They shall exhibit the holder's name and number of shares and shall be signed by the Chairman of the Board, the President or a Vice President and also by the Treasurer or an Assistant Treasurer or the Secretary or an Assistant Secretary and shall bear the corporate seal or a facsimile thereof. If a certificate is countersigned by a transfer agent or registrar, other than the Company itself or its employe, any other signature or countersignature on the certificate may be facsimiles. In case any officer of the Company, or any officer or employe of the transfer agent or registrar, who has signed or whose facsimile

signature has been placed upon such certificate ceases to be an officer of the Company, or an officer or employe of the transfer agent or registrar, before such certificate is issued, said certificate may be issued with the same effect as if the officer of the Company, or the officer or employe of the transfer agent or registrar, had not ceased to be such at the date of issue.

SECTION 6.2. Transfer of Stock. Upon surrender to the Company of a certificate for shares duly endorsed or accompanied by proper evidence of succession, assignment or authority to transfer, and upon payment of applicable taxes with respect to such transfer, it shall be the duty of the Company, subject to such rules and regulations as the Board of Directors may from time to time deem advisable concerning the transfer and registration of certificates for shares of stock of the Company, to issue a new certificate to the person entitled thereto, cancel the old certificate and record the transaction upon its books.

SECTION 6.3. Shareholders of Record. The Company shall be entitled to treat the holder of record of any share or shares of stock as the holder in fact thereof and, accordingly, shall not be bound to recognize any equitable or other claim to or interest in such share or shares on the part of any other person, whether or not it shall have express or other notice thereof, except as otherwise provided by statute.

SECTION 6.4. Lost, Destroyed or Stolen Certificates. The Board of Directors, in individual cases or by general resolution, may direct a new certificate or certificates to be issued by the Company

as a replacement for a certificate or certificates for a like number of shares alleged to have been lost, destroyed or stolen, upon the making of an affidavit of that fact by the person claiming the certificate or certificates of stock to be lost, destroyed or stolen. When authorizing such issue of a new certificate or certificates, the Board of Directors may, in its discretion and as a condition precedent to the issuance thereof, require the owner of such lost, destroyed or stolen certificate or certificates, or his legal representative, to give the Company a bond in such form and amount as it may direct as indemnity against any claim that may be made against the Company with respect to the certificate or certificates alleged to have been lost, destroyed or stolen.

#### ARTICLE VII

##### Miscellaneous

SECTION 7.1. Contracts and Other Instruments. All contracts or obligations of the Company shall be in writing and shall be signed either by the Chairman of the Board, the President, any Executive Vice President, any Vice President, the Treasurer, or any other officer of the Company, agent, employe or attorney-in-fact as may be designated by the Board, the Chairman of the Board or the President pursuant to specific authorizations and, the seal of the Company may be attached thereto, duly attested by the Secretary or an Assistant Secretary, except contracts entered into in the ordinary course of business where the amount involved is less than One Hundred Thousand Dollars (\$100,000), and except contracts for the employment of servants or agents, which contracts so excepted may be entered into by the Chairman of the Board, the President, any Executive Vice

President, any Vice President, the Treasurer, or by such officers, agents, employees or attorneys-in-fact as the Chairman of the Board or the President may designate and authorize. Unless the Board shall otherwise determine and direct, all checks or drafts and all promissory notes shall be signed by two officers of the Company. When prescribed by the Board, bonds, promissory notes, and other obligations of the Company may bear the facsimile signature of the officer who is authorized to sign such instruments and, likewise, may bear the facsimile signature of the Secretary or an Assistant Secretary.

SECTION 7.2. Voting Stock Owned by Company. Any or all shares of stock owned by the Company in any other corporation, and any or all voting trust certificates owned by the Company calling for or representing shares of stock of any other corporation, may be voted by the Chairman of the Board, the President, any Vice President, the Secretary or the Treasurer, either in person or by written proxy given to any person in the name of the Company at any meeting of the shareholders of such corporation, or at any meeting of voting trust certificate holders, upon any question that may be presented at any such meeting. Any such officer, or anyone so representing him by written proxy, may on behalf of the Company waive any notice of any such meeting required by any statute or by-law and consent to the holding of such meeting without notice.

#### ARTICLE VIII

##### Amendment or Repeal of By-Laws

These by-laws may be added to, amended or repealed at any regular or special meeting of the Board by a vote of a majority of the membership of the Board.

---

---

# FORM 10-K

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

Exhibit AA

(Mark One)

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 1989

OR

☐ TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d)  
OF THE SECURITIES EXCHANGE ACT OF 1934

Commission File Number 2-35965

## NORTH SHORE GAS COMPANY

(Exact name of registrant as specified in its charter)

Illinois

(State or other jurisdiction of  
incorporation or organization)

36-1558720

(IRS Employer  
Identification No.)

122 South Michigan Avenue, Chicago, Illinois

(Address of principal executive offices)

60603

(Zip Code)

Registrant's telephone number, including area code:

(312) 431-4000

Securities registered pursuant to Section 12(b) of the Act: None

Securities registered pursuant to Section 12(g) of the Act: None

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No   

State the aggregate market value of the voting stock held by non-affiliates of the registrant:

Redeemable Cumulative Preferred Stock, \$3,000,000 at November 30, 1989, based on the price at which the stock was sold.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, without par value, 3,625,887 shares outstanding at November 30, 1989.

Documents Incorporated by Reference  
None

## CONTENTS

<u>Item No.</u>		<u>Page No.</u>
	<u>Part I</u>	
1.	Business	3
2.	Properties	8
3.	Legal Proceedings	8
4.	Submission of Matters to a Vote of Security Holders	8
	<u>Part II</u>	
5.	Market for the Company's Common Stock and Related Stockholder Matters	8
6.	Selected Financial Data	9
7.	Management's Discussion and Analysis of Results of Operations and Financial Condition	10
8.	Financial Statements and Supplementary Data	12
9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	32
	<u>Part III</u>	
10.	Directors and Executive Officers of the Company	33
11.	Executive Compensation	35
12.	Security Ownership of Certain Beneficial Owners and Management	35
13.	Certain Relationships and Related Transactions	35
	<u>Part IV</u>	
14.	Exhibits, Financial Statement Schedules, and Reports on Form 8-K	36
	Signatures	45
	Exhibit Index	46



North Shore Gas Company

ANNUAL REPORT ON FORM 10-K

FISCAL YEAR ENDED SEPTEMBER 30, 1989

PART I

ITEM 1. BUSINESS

GENERAL

North Shore Gas Company (Company) is an operating public utility engaged primarily in the purchase, storage, distribution, sale, and transportation of natural gas. It has more than 114,000 residential, commercial, and industrial retail sales and transportation customers within its service area of approximately 275 square miles, located in northeastern Illinois. It serves 56 communities and adjacent areas, including those situated along Lake Michigan from Winnetka, Illinois, to the Illinois-Wisconsin state line. This area, with an estimated population of 397,000, contains residential concentrations and a diversity of industrial and commercial establishments, as well as some farm lands. The Company had 243 employees at September 30, 1989.

The Company holds certificates of public convenience and necessity issued by the Illinois Commerce Commission (Commission) for the conduct by the Company of its operations in the territory it serves. It holds a license agreement from Lake County, Illinois, and, with minor exceptions, franchises from all of the incorporated cities and villages in its service territory. The franchises are of various terms and expiration dates and are generally subject to various other conditions, restrictions, or limitations not deemed materially burdensome.

At September 30, 1989, the common stock of the Company and of its affiliate, The Peoples Gas Light and Coke Company (Peoples Gas), was wholly owned by Peoples Energy Corporation (Peoples Energy).

COMPETITION

Competition in varying degrees exists between natural gas and other fuels or forms of energy available to consumers in the Company's service area. Natural gas prices increased during the last year; however, on balance, gas prices have remained competitive in the Company's service area. Overall, natural gas prices in the Company's service area compared very favorably on a national basis.

An increasing number of the customers of the Company are substituting customer-owned gas for gas purchases from the Company, utilizing the availability of pipeline transportation as well as the Company's own transportation service. Under existing rates, the Company experiences no loss of distribution margin due to customer shifts from gas service to transportation service. The Company has utilized the increased availability of open-access transportation to make purchases in the competitive spot market, thereby reducing the average cost of gas that must be recovered from customers.

## ITEM 1. BUSINESS (Continued)

### COMPETITION (Continued)

Despite the access to spot market supplies afforded by open-access transportation, the Company is concerned because it is not known how the changing use of pipeline services under the new open-access rules will affect the security and reliability of long-term supplies from pipelines for distributors.

A pipeline may seek to provide transportation service directly to end-users. Such direct service by a pipeline to an end-user would bypass the local distributor's service and reduce the distributor's earnings. However, to the best of the Company's knowledge, no such service has been proposed for any customers of the Company.

### SALES AND RATES

The Company sells natural gas having an average heating value of approximately 1,000 British thermal units (Btu's) per cubic foot.\* Sales are made and service rendered by the Company pursuant to a rate schedule on file with the Illinois Commerce Commission (Commission) containing various service classifications largely reflecting customers' different uses and level of consumption. Monthly adjustments to the Gas Charge under the Company's rate schedule provide for the pass-through of increases or decreases in natural gas supplier rates, purchased storage service costs, transportation charges, and liquefied petroleum gas costs. In addition, under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or a current asset (with a contra entry to gas costs), and the fiscal year-end balance is amortized over the 12-month period beginning the following January 1. The Company also is currently recovering take-or-pay costs through the Gas Charge. (See Notes (3) and (16) of the Notes to Consolidated Financial Statements.)

The business of the Company is influenced by seasonal weather conditions because a large element of the Company's customer load consists of space heating. Weather-related deliveries can, therefore, have a significant impact on net income. (For a discussion as to the effect of the seasonal nature of gas sales upon cash flow, see "Liquidity and Capital Resources" in Item 7.)

The basic marketing plan of the Company is to maintain its existing market share in all market segments and develop market opportunities emerging from changes in market environment and technology advances in new, expanded, or current natural gas applications.

### STATE LEGISLATION AND REGULATION

The Company is subject to the jurisdiction of and regulation by the Illinois Commerce Commission (Commission), which has general supervisory and regulatory powers over practically all phases of the public utility business in Illinois, including rates and charges, issuance of securities, services and facilities, systems of accounts, investments, safety standards, transactions with affiliated interests, as defined in the Illinois Public Utilities Act, and other matters.

---

\* All volumes of natural gas set forth in this report are stated on a 1,000 Btu (per cubic foot) billing basis.

ITEM 1. BUSINESS (Continued)

STATE LEGISLATION AND REGULATION (Continued)

Under the Illinois Residential Affordable Payment Program (IRAPP), the Company was prohibited from discontinuing gas service to any participating customer who paid the monthly obligation required by IRAPP. The statutory authority authorizing IRAPP expired on October 31, 1989. New energy assistance programs in lieu of IRAPP became effective November 1, 1989. (See Note (1)k of Notes to Consolidated Financial Statements.)

FEDERAL LEGISLATION AND REGULATION

By Order entered on December 6, 1968 (Holding Company Act Release No. 16233), the Securities and Exchange Commission (SEC), pursuant to Section 3(a)(1) of the Public Utility Holding Company Act of 1935 (Act) exempted Peoples Energy and its subsidiary companies as such (including the Company) from the provisions of the Act other than Section 9(a)(2) thereof.

In September 1989, the Federal Energy Regulatory Commission (FERC) order that purported to raise ceiling prices for "old" gas found before 1975 (Order No. 451) was overturned. The appeals court determined that the FERC lacked the statutory authority to issue the Order. The Company supported the court's ruling, which could result in refunds to customers. The FERC, however, has filed a request for rehearing, and it could be some time before the matter is finally resolved.

In October 1989, Order No. 500, a so-called interim order issued in 1987 that promotes transportation of gas into traditional sales markets served by interstate pipelines, was remanded to the FERC by the U.S. Court of Appeals. The Court directed the FERC to issue a final order within 60 days of the remand. The final order must address legal flaws in Order No. 500, including the manner in which the FERC has handled pipeline take-or-pay obligations to producers. As with Order No. 451, the Company was among those that sought this court review. As of now, we do not expect either court action to have a material effect on our operations or gas pricing for the near future.

On July 1, 1988, Natural petitioned the FERC for a rate increase, of which approximately \$4 million would have been passed on to the Company. The request was part of a filing that also proposed seasonal rates. Under this plan, rates for delivery of gas to the pipeline's customers would be significantly higher from November through March than from April through October. In 1989, the parties settled all issues regarding Natural's filing. The settlement rates resulted in a \$1 million annual increase in the cost of service to the Company. The settlement also included a number of non-rate features beneficial to the Company, notably with respect to improving Natural's transportation services.

ENVIRONMENTAL MATTERS

See Note (4) of the Notes to Consolidated Financial Statements.

ITEM 1. BUSINESS (Continued)

GAS SUPPLY ADVANCES AND INVESTMENTS

During the natural gas shortage of the 1970's, the Company undertook several programs to augment its gas supply. From 1973 through 1975, the Company, with Commission approval, made equity investments in development ventures. At September 30, 1989, \$309,000 in equity investments remained outstanding. The Company is allowed by the Commission to include such investments in its rate base and treat any profits or losses as utility transactions. (See Note (14) of Notes to Consolidated Financial Statements for information on the Company's exploration subsidiary.)

CURRENT GAS SUPPLY

The following tabulation shows the expected peak-day availability of gas in million cubic feet (MMcf) during the 1989-90 heating season:

<u>Source</u>	<u>Peak-Day Availability (MMcf)</u>	<u>Year of Contract Expiration</u>
Flow Gas		
Natural Gas Pipeline.....	135	1990 (a)
Company-Liquefied Petroleum Gas.....	60	
	<u>195</u>	
Storage Gas		
Natural Gas Pipeline.....	97 (b)	1990-1995 (a)
Peoples Gas-Manlove Storage.....	87 (c)	1990
	<u>184</u>	
Total expected peak-day availability....	<u>379</u>	

- (a) The flow gas and certain storage contracts with Natural Gas Pipeline Company of America (Natural) are for an initial term expiring November 30, 1990, and year-to-year thereafter, subject to cancellation by either party by one year's written notice. On December 1, 1989, Natural gave written notice to the Company of its cancellation of these contracts, effective November 30, 1990. The Company is negotiating the terms of new flow gas and storage contracts with Natural. In any event, Natural may not terminate service under the expiring agreements without first receiving prior authorization from the FERC.
- (b) The Company has storage service withdrawals available from Natural of (1) 53 MMcf per day subject to maximum seasonal withdrawal of 30 times the maximum daily withdrawal under a service agreement extending to 1990, (2) 30 MMcf per day under a service agreement expiring in 1990, (3) 4 MMcf per day in the peak month, which is January, under a service agreement extending to 1991, (4) 7 MMcf per day under a service agreement extending to 1992, and (5) 3 MMcf per day under a service agreement extending to 1995.
- (c) The Company has a gas storage agreement with Peoples Gas that provides a maximum withdrawal of 87 MMcf of storage service per day. The agreement also makes available additional quantities, if available, equal to the Company's pro rata share.

ITEM 1. BUSINESS (Continued)

CURRENT GAS SUPPLY (Continued)

The Company's sources of gas supply (including gas transported for customers) in million cubic feet (MMcf) for the three fiscal years ended September 30, 1989, 1988, and 1987 were as follows:

	<u>1989</u>	<u>1988</u>	<u>1987</u>
Source:			
Natural (a)	18,664	18,315	11,330
Other Suppliers (a)	7,959	9,173	15,470
Liquefied Petroleum Gas Produced	5	12	5
Customer Owned Gas - Received	8,543	7,045	4,390
Underground Storage - Net	(87)	(247)	255
Company Use, Franchise Requirements and Unaccounted for Gas	<u>(392)</u>	<u>(337)</u>	<u>(287)</u>
Total (b)	<u>34,692</u>	<u>33,961</u>	<u>31,163</u>

( ) Denotes red figure.

- (a) The Company purchases significant quantities of its gas supplies in the competitive spot market, substituting these supplies for more expensive pipeline supplies. Such purchases are made on a month-to-month basis whenever they produce a savings in gas costs without jeopardizing supply security and reliability.
- (b) The lower total deliveries in 1987 were due primarily to warmer weather.

## ITEM 2. PROPERTIES

All of the principal plants and properties of the Company have been maintained in the ordinary course of business and are believed to be in satisfactory operating condition. The following is a brief description of the principal plants and operating units of the Company.

The distribution system of the Company, as of September 30, 1989, consisted of 1,800 miles of distribution mains and necessary pressure regulators, approximately 105,000 services (pipe connecting the mains with piping on the customers' premises), and approximately 117,000 meters installed on customers' premises. The Company has liquefied petroleum gasification and storage facilities. It also owns and has a substantial investment in office and service buildings, garages, repair shops, and motor vehicles, together with the equipment, tools, and fixtures necessary to conduct utility business.

Most of the principal plants and properties of the Company, other than mains, services, meters, regulators, and cushion gas in underground storage, are located on property owned in fee. Substantially all gas mains are installed in public streets, alleys, and highways, or under property owned by others under grants of easements. Meters and house regulators in use and a portion of services are located on premises being served.

Substantially all of the physical properties now owned or hereafter acquired by the Company are subject to (a) the direct, first mortgage lien of the Company's Mortgage to the Continental Illinois National Bank and Trust Company of Chicago, Trustee, to secure the principal amount of the Company's outstanding First Mortgage Bonds and (b) in certain cases, other exceptions and defects that do not interfere with the use of the property.

## ITEM 3. LEGAL PROCEEDINGS

See "Sales and Rates" in Item 1 of this Report.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

## PART II

## ITEM 5. MARKET FOR THE COMPANY'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The Company is a wholly owned subsidiary of Peoples Energy.

# ITEM 6. SELECTED FINANCIAL DATA (a)

For fiscal years ended September 30,	1989	1988	1987	1986	1985
<b>OPERATING RESULTS (thousands)</b>					
Operating Revenues:					
Residential	\$ 93,055	\$ 84,320	\$ 81,450	\$ 96,265	\$ 99,472
Commercial	26,616	27,546	31,229	38,133	40,837
Industrial	5,655	6,017	12,164	30,409	34,052
Transportation of customer-owned gas	7,404	4,990	2,523	7	--
Other	904	840	792	944	966
Total Operating Revenues	<u>133,634</u>	<u>123,713</u>	<u>128,158</u>	<u>165,758</u>	<u>175,327</u>
Less - Gas costs	80,203	71,708	77,616	108,893	118,789
- Revenue taxes	8,524	7,828	8,591	11,094	12,026
Net Operating Revenues	<u>\$ 44,907</u>	<u>\$ 44,177</u>	<u>\$ 41,951</u>	<u>\$ 45,771</u>	<u>\$ 44,512</u>
Net Income Applicable to Common Stock	\$ 10,104(b)	\$ 9,780	\$ 7,183	\$ 8,900	\$ 8,782
Dividends declared on common stock	\$ 4,786	\$ 3,699	\$ 3,517	\$ 5,802	\$ 6,671
<b>ASSETS (thousands)</b>					
Property, plant and equipment	\$176,222	\$163,985	\$151,020	\$138,601	\$128,767
Less - Accumulated depreciation	56,558	52,573	48,640	45,299	41,803
Net Property, Plant and Equipment	<u>\$119,664</u>	<u>\$111,412</u>	<u>\$102,380</u>	<u>\$ 93,302</u>	<u>\$ 86,964</u>
Capital expenditures - construction	\$ 13,714	\$ 14,144	\$ 14,539	\$ 10,810	\$ 8,072
Total Assets	<u>\$152,368</u>	<u>\$142,442</u>	<u>\$131,802</u>	<u>\$123,957</u>	<u>\$130,756</u>
<b>CAPITALIZATION AT YEAR-END (thousands)</b>					
Common equity	\$ 59,360	\$ 54,042	\$ 47,961	\$ 44,295	\$ 41,197
Preferred stock	3,000	3,000	3,000	3,000	4,000
Long-term debt	36,754	39,345	23,525	27,625	33,082
Total	<u>\$ 99,114</u>	<u>\$ 96,387</u>	<u>\$ 74,486</u>	<u>\$ 74,920</u>	<u>\$ 78,279</u>
<b>CAPITALIZATION RATIOS AT YEAR-END (per cent)</b>					
Common equity	60	56	64	59	53
Preferred stock	3	3	4	4	5
Long-term debt	37	41	32	37	42
Total	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>
<b>GAS SOLD AND TRANSPORTED (million cubic feet)</b>					
Residential	19,070	18,640	16,670	18,161	17,209
Commercial	5,987	6,870	7,288	8,090	7,946
Industrial	1,248	1,478	2,956	6,806	6,867
Transportation of customer-owned gas	8,387	6,973	4,249	19	--
Total	<u>34,692</u>	<u>33,961</u>	<u>31,163</u>	<u>33,076</u>	<u>32,022</u>
<b>NUMBER OF CUSTOMERS (average)</b>					
Residential	106,138	102,906	99,537	96,281	94,393
Commercial	6,496	6,245	6,241	5,962	5,769
Industrial	682	713	704	717	700
Transportation	878	437	52	1	--
Total	<u>114,194</u>	<u>110,301</u>	<u>106,534</u>	<u>102,961</u>	<u>100,862</u>
<b>DEGREE DAYS</b>					
	6,555	6,436	5,760	6,747	6,650
Per cent of normal (6,455)	102	100	89	105	103

(a) The Company is a wholly owned subsidiary of Peoples Energy; therefore, per share data are omitted.

(b) Includes the cumulative effect of an accounting change of \$0.9 million, net of income taxes of \$0.6 million. (See Note (1)b of Notes to Consolidated Financial Statements.)

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS  
AND FINANCIAL CONDITION

Results of Operations

Gross revenues have been affected in recent years by the election of some customers to purchase gas directly from producers and brokers, rather than from the Company, and also by changes in the unit cost of gas purchased by the Company. These two factors, however, have no direct effect on net income. With respect to customers' purchase of gas from producers and brokers, the Company transports customer-owned gas to end users and recovers margins similar to those from conventional gas sales. Also, changes in the unit cost of gas do not directly affect net income because the Company's tariffs provide for dollar-for-dollar recovery of gas costs. (See Note (1)i of Notes to Consolidated Financial Statements.) Since income is not directly affected by these factors, the discussion below pertains to "net operating revenues," which the Company considers a more pertinent measure of operating results than gross revenues.

Weather variations affect the volumes of gas delivered for heating and, therefore, can have a significant impact on net income.

Since utility properties are reported and recovered through rates at historical cost, the potentially material effect of inflation and changing prices is not reflected in the consolidated financial statements.

Income from operations before the cumulative effect of an accounting change decreased \$0.6 million in 1989, due principally to higher operating costs mainly for employee benefits. Offsetting items were the recovery in 1989 from the State of Illinois of certain costs incurred in prior years pertaining to a state-imposed customer assistance program (See Note (1)k of Notes to Consolidated Financial Statements), and income tax adjustments. The cumulative effect of the accounting change, effective October 1, 1988, to accrue unbilled revenues resulted in an increase in net income of \$0.9 million, net of income taxes, for fiscal 1989. (See Note (1)b of Notes to Consolidated Financial Statements.)

Net income increased by \$2.6 million in 1988, primarily due to increased gas deliveries significantly influenced by weather that was relatively normal compared to very warm weather in the previous year, and a lower federal income tax rate as a result of the Tax Reform Act of 1986. The net income effect of these factors were tempered by a refund and rate reduction. (See Note (3) of Notes to Consolidated Financial Statements.)

A summary of significant variations in income is presented below, with explanations following:

(Thousands of dollars)	Fiscal 1989 Over 1988		Fiscal 1988 Over 1987	
	Amount	%	Amount	%
Net operating revenues*	\$ 730	1.7	\$2,226	5.3
Operation and maintenance expenses	1,494	8.4	(991)	(5.3)
Income taxes	(707)	(11.4)	(156)	(2.5)
Other income	(163)	(14.4)	543	92.3
Income deductions	(251)	(4.9)	1,056	26.3
Income before cumulative effect of accounting change	(576)	(5.9)	2,597	36.2
Cumulative effect of accruing unbilled revenues, net of income taxes	900	--	--	--
Net Income Applicable to Common Stock	324	3.3	2,597	36.2

( ) Denotes red figure.

\* Operating revenues net of gas costs and revenue taxes.



ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS  
AND FINANCIAL CONDITION (Continued)

Results of Operations (Continued)

The increase in net operating revenues in 1989 was mainly the result of a recovery of certain costs incurred in prior years pertaining to a state-imposed customer assistance program. (See Note 1(k) of Notes to Consolidated Financial Statements.) Primary reasons for the increase in 1988 were relatively normal weather in 1988 compared to a very warm 1987, and increased customer demand.

Operation and maintenance expenses increased in 1989 due to several factors, including increased costs for employee welfare benefits and an increase in the provision for uncollectible accounts. In 1988, operation and maintenance expenses decreased, chiefly due to a favorable settlement involving advance payments for gas supply exploration.

Income taxes decreased in 1989, as compared to 1988, principally due to the effect of a 1989 adjustment of deferred taxes and out-of-period items in 1988 at different tax rates. Income taxes were down slightly in 1988 from 1987 as a result of the lower federal income tax rate, which was substantially offset by higher pre-tax income and the out-of-period items referred to above.

The variations in other income from year-to-year mainly reflect the amount of cash available for short-term investments and interest rates.

Income deductions were down in 1989, primarily due to a reduction in interest on amounts refundable to customers. Income deductions increased in 1988, mainly due to the interest on the \$20 million ten-year First Mortgage Bonds, 10.20% Series I, issued on December 1, 1987.

Liquidity and Capital Resources

The Company has access to outside capital markets and to internal sources of funds that together should provide sufficient resources to meet capital requirements. It does not anticipate any changes that materially would alter its current liquidity position.

Due to the seasonal nature of gas deliveries for space heating, a major portion of cash collections occurs between November and April. Because of timing differences in the receipt and disbursement of cash, and the level of construction requirements, the Company may borrow on a short-term basis. Short-term borrowings are either repaid with cash from operations or refinanced on a permanent basis with debt or equity, depending on money-market conditions and capital structure considerations.

Net cash provided by operating activities increased in 1989 primarily due to higher net income, the recovery of prior-period IRAPP and take-or-pay costs, and a reduction in the net amounts refundable to customers. Net cash provided by operating activities decreased in 1988 due mainly to adjustments resulting from the Tax Reform Act of 1986, substantially offset by higher net income. Net cash used in investing activities for 1989, 1988, and 1987 principally represents the level of capital expenditures in the respective years. Changes in net cash from investing activities mainly reflect the issuance of additional long-term debt in 1988 and year-to-year variations in interim loan activity.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS  
AND FINANCIAL CONDITION (Continued)

Liquidity and Capital Resources (Continued)

Additional bonds are issuable by the Company, upon Illinois Commerce Commission approval, subject to limitations by certain restrictive provisions of the open-end mortgages and supplements thereto. These restrictions are not expected to have an impact on the Company's ability to issue additional debt, as needed. The Company does not expect to issue any new long-term debt in fiscal 1990. Short-term cash needs are met through borrowing arrangements with banks and/or the issuance of commercial paper. At September 30, 1989, the Company had unused credit available from banks of \$15 million. (See Note (11) of Notes to Consolidated Financial Statements.) The commercial paper of the Company enjoys the top rating from leading rating agencies.

The Company's coverage of fixed charges, before the cumulative effect of an accounting change, for fiscal 1989, 1988, and 1987 was 4.11, 4.20, and 4.45, respectively. The long-term debt of the Company is rated Aa3 by Moody's Investors Service and AA- by Standard and Poor's Corporation. There has been no change in either of these ratings since fiscal 1985.

Capital expenditures for additions, replacements, and improvements to the utility plant were \$13.7 million in 1989, \$14.1 million in 1988, and \$14.5 million in 1987. Capital expenditures for fiscal 1990 are estimated to be \$13.6 million.

In December 1987, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 96, "Accounting for Income Taxes." The impact of the future adoption of SFAS No. 96 on the financial position of the Company is not expected to be significant. (See Note (1)g of Notes to Consolidated Financial Statements.)

The Company is conducting an environmental investigation of certain sites that were the location of former gas manufacturing operations. (See Note (4) of Notes to Consolidated Financial Statements.)

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

	<u>Page</u>
Report of Independent Public Accountants	13
Consolidated Statements of Income for fiscal years ended September 30, 1989, 1988, and 1987	14
Consolidated Statements of Retained Earnings for fiscal years ended September 30, 1989, 1988, and 1987	14
Consolidated Balance Sheets as of September 30, 1989, and 1988	15
Consolidated Capitalization Statements as of September 30, 1989, and 1988	16
Consolidated Statements of Cash Flows for fiscal years ended September 30, 1989, 1988, and 1987	17
Notes to Consolidated Financial Statements	18
Selected Quarterly Financial Data	31

## REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To North Shore Gas Company:

We have audited the accompanying consolidated balance sheets and consolidated capitalization statements of North Shore Gas Company (an Illinois corporation, hereinafter referred to as the Company and a wholly owned subsidiary of Peoples Energy Corporation) and subsidiary companies as of September 30, 1989 and 1988, and the related consolidated statements of income, retained earnings, and cash flows for each of the three years in the period ended September 30, 1989. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the Company and subsidiary companies at September 30, 1989 and 1988, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 1989, in conformity with generally accepted accounting principles.

As discussed in Note (1)h of the Notes to Consolidated Financial Statements, the method of accounting for pensions was changed in fiscal year 1987.

As discussed in Note (1)b of the Notes to Consolidated Financial Statements, the method of accounting for revenues was changed effective October 1, 1988.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The financial statement schedules listed in Item 14(a)2 are presented for purposes of complying with the Securities and Exchange Commission's rules and are not part of the basic financial statements. These financial statement schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN & CO.

Chicago, Illinois  
November 1, 1989

North Shore Gas Company  
CONSOLIDATED STATEMENTS OF INCOME  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1989	1988	1987
OPERATING REVENUES:			
Gas sales	\$125,326	\$117,883	\$124,843
Transportation of customer-owned gas	7,404	4,990	2,523
Other	904	840	792
Total Operating Revenues	<u>133,634</u>	<u>123,713</u>	<u>128,158</u>
OPERATING EXPENSES:			
Gas costs	80,203	71,708	77,616
Operation	16,767	15,468	16,239
Maintenance	2,434	2,239	2,459
Depreciation	5,081	4,808	4,541
Taxes - Income	5,478	6,185	6,341
- State and local revenue	8,524	7,828	8,591
- Other	1,820	1,486	1,461
Total Operating Expenses	<u>120,307</u>	<u>109,722</u>	<u>117,248</u>
OPERATING INCOME	<u>13,327</u>	<u>13,991</u>	<u>10,910</u>
OTHER INCOME:			
Interest income	574	927	331
Allowance for funds used during construction	176	114	25
Miscellaneous	218	90	232
Total Other Income	<u>968</u>	<u>1,131</u>	<u>588</u>
GROSS INCOME	<u>14,295</u>	<u>15,122</u>	<u>11,498</u>
INCOME DEDUCTIONS:			
Interest on long-term debt	4,058	4,190	2,962
Other interest	725	848	1,032
Amortization of debt discount and expense	38	34	21
Miscellaneous	--	--	1
Total Income Deductions	<u>4,821</u>	<u>5,072</u>	<u>4,016</u>
INCOME BEFORE CUMULATIVE EFFECT OF ACCOUNTING CHANGE	9,474	10,050	7,482
Cumulative effect of accruing unbilled revenues, net of income taxes	<u>900</u>	<u>--</u>	<u>--</u>
NET INCOME	10,374	10,050	7,482
Preferred stock dividends	<u>270</u>	<u>270</u>	<u>299</u>
NET INCOME APPLICABLE TO COMMON STOCK	<u>\$ 10,104</u>	<u>\$ 9,780</u>	<u>\$ 7,183</u>

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1989	1988	1987
BALANCE AT BEGINNING OF YEAR	\$ 29,285	\$ 23,204	\$ 19,538
Add - Net Income	10,374	10,050	7,482
Deduct - Dividends on common stock	4,786	3,699	3,517
- Dividends on preferred stock	270	270	299
BALANCE AT END OF YEAR	<u>\$ 34,603</u>	<u>\$ 29,285</u>	<u>\$ 23,204</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company  
CONSOLIDATED BALANCE SHEETS  
(Thousands of Dollars)

	As of September 30,	
	<u>1989</u>	<u>1988</u>
<b>PROPERTIES AND OTHER ASSETS</b>		
<b>CAPITAL INVESTMENTS:</b>		
Property, plant and equipment, at original cost	\$176,222	\$163,985
Less - Accumulated depreciation	<u>56,558</u>	<u>52,573</u>
	119,664	111,412
Gas supply advances and investments	309	432
<b>TOTAL CAPITAL INVESTMENTS</b>	<u>119,973</u>	<u>111,844</u>
<b>CURRENT ASSETS:</b>		
Cash	831	415
Cash equivalents	--	2,500
Receivables -		
Customers, net of allowance for uncollectible accounts of \$620 and \$646, respectively	3,478	3,486
Other	82	29
Accrued unbilled revenues	2,219	--
Materials and supplies, at average cost	2,331	2,300
Gas in storage, at last-in, first-out cost	19,686	19,686
Gas costs recoverable through rate adjustments	2,177	135
Prepayments	375	489
<b>TOTAL CURRENT ASSETS</b>	<u>31,179</u>	<u>29,040</u>
<b>DEFERRED CHARGES</b>	<u>1,216</u>	<u>1,558</u>
<b>TOTAL PROPERTIES AND OTHER ASSETS</b>	<u>\$152,368</u>	<u>\$142,442</u>
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION</b> (see accompanying statement)	<u>\$ 99,114</u>	<u>\$ 96,387</u>
<b>CURRENT LIABILITIES:</b>		
Interim loans	5,000	--
Accounts payable	7,860	7,441
Dividends payable on common stock	616	1,341
Customer deposits	5,668	5,790
Sinking fund payments and maturities -		
Long-term debt	2,194	2,100
Accrued taxes	1,776	1,136
Gas sales revenue refundable	5,817	5,274
Accrued interest	1,064	1,067
<b>TOTAL CURRENT LIABILITIES</b>	<u>29,995</u>	<u>24,149</u>
<b>RESERVES AND DEFERRED CREDITS:</b>		
Deferred income taxes - primarily accelerated depreciation	17,449	16,318
Investment tax credits being amortized over the average lives of related property	4,813	4,967
Other	997	621
<b>TOTAL RESERVES AND DEFERRED CREDITS</b>	<u>23,259</u>	<u>21,906</u>
<b>TOTAL CAPITALIZATION AND LIABILITIES</b>	<u>\$152,368</u>	<u>\$142,442</u>

( ) Denotes red figure.

The accompanying notes are an integral part of these statements.

North Shore Gas Company

CONSOLIDATED CAPITALIZATION STATEMENTS  
(Thousands of Dollars)

	<u>As of September 30,</u>	
	<u>1989</u>	<u>1988</u>
COMMON STOCKHOLDER'S EQUITY:		
Common stock, without par value -		
Authorized 5,000,000 shares,		
Outstanding 3,625,887 shares	\$ 24,757	\$ 24,757
Retained earnings (see accompanying statement)	<u>34,603</u>	<u>29,285</u>
TOTAL COMMON STOCKHOLDER'S EQUITY	<u>59,360</u>	<u>54,042</u>
REDEEMABLE CUMULATIVE PREFERRED STOCK:		
Exclusive of sinking fund payments, due within one year		
Authorized 190,000 shares, par value \$100 -		
9% Series, 30,000 shares outstanding	<u>3,000</u>	<u>3,000</u>
TOTAL REDEEMABLE CUMULATIVE PREFERRED STOCK	<u>3,000</u>	<u>3,000</u>
LONG-TERM DEBT:		
Exclusive of sinking fund payments and maturities,		
due within one year		
First Mortgage Bonds -		
9-1/2% Series E, due February 1, 1995	5,875	6,101
8-3/8% Series F, due October 1, 1998	6,679	6,944
8-3/8% Series G, due February 15, 1992	1,200	1,800
12% Series H, due September 15, 1995	3,000	4,500
10.20% Series I, due October 27, 1997	<u>20,000</u>	<u>20,000</u>
TOTAL LONG-TERM DEBT	<u>36,754</u>	<u>39,345</u>
TOTAL CAPITALIZATION	<u>\$ 99,114</u>	<u>\$ 96,387</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Thousands of Dollars)

	<u>For Fiscal Years Ended September 30,</u>		
	<u>1989</u>	<u>1988</u>	<u>1987</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net Income	<u>\$ 10,374</u>	<u>\$ 10,050</u>	<u>\$ 7,482</u>
Adjustments to reconcile net income to net cash:			
Depreciation	5,081	4,808	4,541
Deferred income taxes and investment tax credits - net	972	585	670
Change in deferred credits - refund to customers	--	(678)	678
Change in other deferred credits and reserves	380	(149)	3
Change in deferred charges	343	(715)	(61)
Amortization	124	136	207
Change in certain current assets and liabilities:			
Receivables - net	(45)	652	1,392
Accrued unbilled revenues	(2,219)	--	--
Payables	419	238	(300)
Gas in storage	--	(632)	1,082
Rate adjustments refundable or recoverable	(1,499)	(3,788)	(896)
Accrued taxes	640	1,351	(1,306)
Customer deposits	(121)	709	262
Materials and supplies	(31)	(613)	(291)
Other	<u>111</u>	<u>961</u>	<u>(221)</u>
Total adjustments	<u>4,155</u>	<u>2,865</u>	<u>5,760</u>
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<u>14,529</u>	<u>12,915</u>	<u>13,242</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Capital expenditures - construction	(13,714)	(14,144)	(14,539)
Other assets	380	305	919
Recovery of advance payments for gas supply	<u>--</u>	<u>789</u>	<u>--</u>
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<u>(13,334)</u>	<u>(13,050)</u>	<u>(13,620)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Retirement of long-term debt	(2,497)	(4,419)	(5,468)
Retirement of preferred stock	--	--	(1,000)
Interim loans - net	5,000	(11,500)	11,500
Issuance of long-term debt	--	20,000	--
Dividends paid on preferred stock	(270)	(270)	(310)
Dividends paid on common stock	<u>(5,512)</u>	<u>(2,357)</u>	<u>(3,517)</u>
<b>NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES</b>	<u>(3,279)</u>	<u>1,454</u>	<u>1,205</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	<u>(2,084)</u>	<u>1,319</u>	<u>827</u>
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<u>2,915</u>	<u>1,596</u>	<u>769</u>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<u>\$ 831</u>	<u>\$ 2,915</u>	<u>\$ 1,596</u>

( ) Denotes red figure.

The accompanying notes are an integral part of these statements.

# North Shore Gas Company

## STATEMENT OF MANAGEMENT

These financial statements were prepared by management, which is responsible for their integrity and objectivity. The statements are in conformity with generally accepted accounting principles and necessarily include some amounts that are based on the best estimates and judgments of management.

Based upon the Company's accounting and internal control systems, along with ongoing internal audit programs, management believes that the accounting records are reliable for the purpose of preparing financial statements, and assets are appropriately safeguarded against loss from unauthorized use.

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### (1) SIGNIFICANT ACCOUNTING POLICIES

#### a. Principles of Consolidation

All subsidiaries of the Company are included in the consolidated financial statements. All significant intercompany transactions have been eliminated in consolidation. Certain items previously reported for years prior to 1989 have been reclassified to conform with the current-year presentation.

#### b. Change in Accounting for Revenues

To match costs and revenues more closely, the Company changed its method of accounting, effective October 1, 1988, to record accrued revenues for all gas delivered at the end of the month. Previously, revenues were recognized when accounts were billed. Revenues related to gas delivered after billing and before the end of a month were recognized in the following month.

The cumulative effect of the accounting change at October 1, 1988, was \$0.9 million, net of income taxes of \$0.6 million. The change had the effect of increasing fiscal 1989 net income (excluding the beginning of the year cumulative effect of \$0.9 million) by \$65,000.

The pro forma effect of this accounting change on net income applicable to common stock, as if the change had been applied retroactively, is as follows:

	Fiscal Years		
	1989	1988	1987
		(000's)	
As Reported	\$10,104	\$ 9,780	\$ 7,183
Pro Forma	\$ 9,204	\$ 9,704	\$ 7,144



North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

c. Statement of Cash Flows

For purposes of the balance sheet and the statement of cash flows, the Company considers all short-term liquid investments with an original maturity of three months or less to be cash equivalents.

Income taxes paid were \$4.8 million, \$4.2 million, and \$6.8 million in fiscal years 1989, 1988, and 1987, respectively. Interest paid (excluding capitalized interest) during the same periods was \$4.5 million, \$3.6 million, and \$3.5 million, respectively.

d. Property, Plant and Equipment

Property, plant and equipment is stated at original cost and includes appropriate amounts of payroll taxes, employee-benefit costs, administrative costs, and an allowance for funds used during construction.

e. Maintenance and Depreciation

The Company charges the cost of maintenance and repairs of property and minor renewals and improvements of property to maintenance expense. When depreciable property is retired, its original cost is charged to the accumulated provision for depreciation.

The provision for depreciation substantially reflects the systematic amortization of the original cost of depreciable property over the estimated useful lives on the straight-line method. Additionally, actual dismantling cost, net of salvage, is included in the provision for depreciation in the month incurred. The amounts provided are designed to cover not only losses due to wear and tear that are not restored by maintenance, but also losses due to obsolescence and inadequacy.

The provision for depreciation, expressed as an annual percentage of original cost of depreciable property, approximated 3.5%, 3.5%, and 3.6% for each of the fiscal years 1989, 1988, and 1987, respectively.

f. Allowance for Funds Used During Construction

The assumed cost of all funds used to finance substantial and lengthy construction is capitalized as a cost element of Utility Plant, with an offsetting credit to Other Income. Under established regulatory practices, the Company is permitted to include in its rates a fair return on, and the recovery of, these capitalized costs by including them in rate base and in the provision for depreciation.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

g. Taxes

For federal and Illinois income tax purposes, for periods prior to January 1, 1981, the Company adopted liberalized methods of computing depreciation on property additions after December 31, 1953, and the Asset Depreciation Range (ADR) system on property additions after December 31, 1970. For periods after December 31, 1980, the Company utilized the Accelerated Cost Recovery System (ACRS), and the Modified Accelerated Cost Recovery System (MACRS) was used on property additions after December 31, 1986.

Deferred income taxes for the difference between tax depreciation computed on these methods and book depreciation are charged to income and credited to accumulated deferred income taxes. This account is charged and income is credited when tax depreciation becomes less than book depreciation.

Investment tax credits have been deferred and are being amortized through credits to income over the book lives of related property. The Tax Reform Act of 1986, signed into law on October 22, 1986, repealed the investment tax credit for property placed in service after December 31, 1985, subject to certain transition rules.

At September 30, 1989, the cumulative net amount of timing differences for which deferred income taxes have been over provided is approximately \$0.8 million.

The preceding deferred-tax and tax-credit accounting conforms with regulations of the Illinois Commerce Commission.

As a result of the Tax Reform Act of 1986, the applicable federal income tax rate for the Company in fiscal 1989 was 34%. The federal income tax rates applied by the Company in fiscal 1988 and 1987 were 34% and 43%, respectively.

The State of Illinois has increased the corporate income tax rate from 4% to 4.8% for the period July 1, 1989, through June 30, 1991. Analysis of the tax bill indicates that the election of a favorable income period allocation method will defer the tax rate increase to fiscal 1990.

In December 1987, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 96, "Accounting for Income Taxes." While earlier application was encouraged, the Company was not required to adopt the new accounting rules until fiscal 1990. In December 1988, the FASB issued SFAS No. 100, "Accounting for Income Taxes - Deferral of Effective Date of FASB No. 96." This statement deferred the effective date of SFAS No. 96 until fiscal 1991. In SFAS No. 96, the FASB retained the existing requirement to record deferred taxes for transactions that are reported

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

g. Taxes (Continued)

in different years for financial reporting and tax purposes. These items, referred to as temporary differences in SFAS No. 96, also included differences between the book and tax bases of assets and liabilities. While comprehensive inter-period income tax allocation continues, the methodology and measurement of deferred income taxes have changed. The impact of SFAS No. 96 on the financial position of the Company is not expected to be significant.

h. Accounting for Pensions

Effective October 1, 1986, the Company adopted the provisions of SFAS No. 87, "Employers' Accounting for Pensions." Pension expense for fiscal 1987 was \$0.8 million as compared to \$1.3 million for fiscal 1986, mainly due to the implementation of SFAS No. 87. (See Note (5) of Notes to Consolidated Financial Statements.)

i. Recovery of Gas Costs

Under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or as a current asset (with a contra entry to gas costs), and the fiscal year-end balance is amortized over the 12-month period beginning the following January 1.

The Company also is currently recovering take-or-pay costs through the Gas Charge. See Note (3) of the Notes to Consolidated Financial Statements.

j. Gas in Storage

Storage injections are priced at the fiscal-year average of costs of natural gas purchased. Withdrawals from storage are priced on the last-in, first-out (LIFO) method. The estimated current replacement cost of gas in inventory, at September 30, 1989, and 1988, exceeded the LIFO cost by approximately \$27 million and \$22 million, respectively.

k. Illinois Residential Affordable Payment Program (IRAPP)

Under IRAPP, which was implemented in December 1985, the Company was prohibited from discontinuing gas service to any participating customer who paid the monthly obligation required by IRAPP (the monthly obligation). For the period December 1 through April 30, the monthly obligation was 8 per cent of the customer's income, and for the period May 1 through November 30, that obligation was the greater of 8 per cent

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

k. Illinois Residential Affordable Payment Program (IRAPP) (Continued)

of the customer's income or the full amount of the customer's current bill calculated under tariff provisions (the current bill). The difference between the current bill and the monthly obligation is referred to as "shortfall."

The Illinois Commerce Commission (Commission) has ruled that IRAPP participants are not at any time required to pay for shortfall. Therefore, accumulated shortfall is excluded from gas sales and is reflected in deferred credits with a corresponding amount in deferred charges. Amounts representing shortfall are recognized as gas sales when recovered from sources other than IRAPP participants (such as governmental assistance programs).

The Illinois General Assembly has appropriated \$40 million to the Illinois Department of Commerce and Community Affairs (DCCA) to reimburse public utilities and other energy vendors for shortfall incurred under IRAPP or similar percentage of income payment plans of other energy vendors. On August 3, 1988, the Commission initiated an investigation to determine the amounts of shortfall incurred under IRAPP through November 30, 1987, by the Company and other public utilities, for the purpose of determining the amount properly payable to each utility. On August 23, 1989, the Commission entered an order finding that the reimbursable shortfall for the investigation period was \$86,000 for the Company. That amount was paid to the Company by DCCA in October 1989. At September 30, 1989, the total accumulated shortfall reflected in the deferred accounts of the Company for the period after November 30, 1987, was \$0.1 million.

On September 7, 1989, the Commission issued an order initiating investigations to determine the amounts properly payable to public utilities, including the Company, for shortfalls incurred under IRAPP during the period of December 1, 1987, through October 31, 1989. Beyond the amounts representing recovery of shortfall through November 30, 1987, the Company cannot reasonably determine at this time the future impact of accumulated shortfall reflected in the deferred accounts.

Under legislation that became effective on August 2, 1989, no assistance is to be provided to participants under IRAPP after October 31, 1989. This legislation also established other energy assistance programs in lieu of IRAPP to be effective November 1, 1989. The new legislation provides for utilities to be compensated by the State of Illinois, generally on a month-to-month basis, for energy assistance extended to participants in the new program.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(2) COVENANTS REGARDING RETAINED EARNINGS

North Shore's Indenture relating to the First Mortgage Bonds and the Stock Purchase Agreements relating to the Cumulative Preferred Stock contain provisions and covenants restricting the payment of cash dividends and the purchase or redemption of capital stock. At September 30, 1989, such restrictions amounted to \$4.3 million out of North Shore's total retained earnings of \$34.6 million.

(3) RATES AND REGULATION

On December 22, 1987, the Illinois Commerce Commission (Commission) approved a filing made by the Company to make effective in January 1988 a one-time refund and implement a rate reduction. The Company refunded \$1.1 million via a credit to its customers' accounts on January 7, 1988, and reduced rates to reflect a reduction in annual operating revenues (excluding additional charges for revenue taxes) of \$2.9 million.

In April 1988, the major pipeline supplier of the Company, Natural Gas Pipeline Company of America (Natural), received permission from the Federal Energy Regulatory Commission (FERC) to recover from its utility customers, including the Company, by separate charges, certain of Natural's so-called "past" take-or-pay costs. These costs arise from the settlement of liabilities under agreements with producers that require Natural to pay for supplies it contracted for, whether or not it takes and subsequently sells them. Natural's recovery of these costs was approved pursuant to a policy adopted by the FERC in Order No. 500.

By an Order dated April 27, 1988, the Commission initiated an investigation into the appropriate recovery by Illinois gas utilities of take-or-pay charges imposed by pipelines pursuant to Order No. 500, and ordered that the utilities defer payments of these costs on their books pending the resolution of this investigation.

Natural began billing these charges in June 1988. Such charges are anticipated to be in effect for a period ending between four to five years from their inception.

On November 22, 1988, the Commission issued an Order allowing state gas utilities, including the Company, to fully recover separate supplier charges for take-or-pay, through the Uniform Gas Charge, from all classes of customers. The Company began recovery of these costs from all its customers, including transportation customers, based on service rendered on and after February 1, 1989. The Commission's November 22, 1988 Order is currently being appealed by certain intervenors to the Illinois Appellate Court. While the Company cannot predict the Appellate Court's decision, the Company believes that the Commission's decision is fully supported by statute and precedent, federal and state, and the evidentiary record and, accordingly, will be upheld on appeal. (See Note (16) of the Notes to Consolidated Financial Statements.)

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(3) RATES AND REGULATION (Continued)

On May 1, 1989, Natural filed an application for authority to institute a Gas Inventory Demand Charges (GIDC) tariff. The tariff would establish new charges to compensate Natural for the costs of maintaining the ability to provide firm sales service up to customers' nominated levels. After negotiations, the parties to this proceeding agreed to an interim settlement that would resolve the GIDC issue through November 30, 1990, which is the date of expiration of Natural's current sales service agreements with Natural's customers. Under the settlement, customers would pay a charge for each unit of shortfall in purchases below a specified threshold amount. Natural would provide a supply warranty, and no other mechanism for recovery of Natural's take-or-pay costs for the November 1989 through November 1990 period could later be applied to customers. The parties await the FERC's decision on the proposed interim settlement.

(4) ENVIRONMENTAL MATTERS

The Company, its predecessors, and certain former affiliates operated facilities in the past for manufacturing gas and storing manufactured gas. In connection with manufacturing and storing gas, various by-products and waste materials were produced, some of which might have been disposed of on sites where the facilities were located. Under certain laws and regulations relating to the protection of the environment, the Company might be required to undertake remedial action with respect to some of these materials if found at the sites. The Company, in conjunction with an environmental consulting firm, is investigating the sites to determine what, if any, remedial action might be necessary. At this time, it is not known whether any remedial action will be necessary at the sites or, if necessary, what the cost of any such action would be. Accordingly, management does not have reason to believe that any such costs will have a material adverse effect on financial position or results of operations of the Company.

(5) PENSION PLANS AND POST-RETIREMENT BENEFITS

The Company participates in two defined benefit pension plans covering substantially all employees. These plans provide pension benefits that generally are based on an employee's length of service, compensation during the five years preceding retirement, and social security benefits. The Company makes annual contributions to the plans based upon actuarial determinations and in consideration of tax regulations and funding requirements under federal law.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(5) PENSION PLANS AND POST-RETIREMENT BENEFITS (Continued)

Net pension cost for fiscal 1989, 1988, and 1987 includes the following components:

	<u>1989</u>	<u>1988</u>	<u>1987</u>
	(Millions)		
Service cost - benefits earned during year	\$ 0.7	\$ 0.7	\$ 0.7
Interest cost on projected benefit obligations	2.0	1.8	1.7
Actual returns on plan assets	(5.0)	--	(4.8)
Net amortization and deferral	<u>3.1</u>	<u>(1.9)</u>	<u>3.2</u>
Net pension cost	<u>\$ 0.8</u>	<u>\$ 0.6</u>	<u>\$ 0.8</u>

The calculation of pension cost assumed a long-term rate of return on assets of 7.0% for 1989 and 1988, and 6.5% for 1987.

The following table shows the estimated funded status of the Company's pension plans at September 30, 1989, and 1988. The projected benefit obligation was determined using weighted average discount rates of 6.9% and 7.6% as of year-end 1989 and 1988, respectively, and assumed future compensation increases of 5.5% for both years. Plan assets consist primarily of marketable equity and fixed-income securities.

	<u>1989</u>	<u>1988</u>
	(Millions)	
Actuarial present value of plan benefits:		
Vested	\$18.9	\$15.7
Non-vested	<u>2.7</u>	<u>1.6</u>
Accumulated benefit obligation	21.6	17.3
Effect of projected future compensation increases	<u>8.0</u>	<u>7.0</u>
Projected benefit obligation	29.6	24.3
Plan assets at market value	<u>32.1</u>	<u>27.7</u>
Plan assets in excess of projected benefit obligation *	<u>\$ 2.5</u>	<u>\$ 3.4</u>
* Comprising:		
Effect of changes in assumptions and difference between actual and estimated experience	\$ 2.0	\$ 2.9
Unrecognized transition asset	<u>0.5</u>	<u>0.5</u>
	<u>\$ 2.5</u>	<u>\$ 3.4</u>

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(5) PENSION PLANS AND POST-RETIREMENT BENEFITS (Continued)

In addition to providing pension benefits, the Company provides certain health-care and life insurance benefits for retired employees. Substantially all employees may become eligible for such benefit coverage if they reach retirement age while working for the Company. The costs of providing these benefits are recognized as an expense during the period in which the costs are incurred. Such costs during fiscal years 1989, 1988, and 1987 were \$284,000, \$216,000, and \$186,000, respectively.



North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(6) TAX MATTERS

Provision for Income Taxes			
For fiscal years ended September 30,			
	1989	1988	1987
	(000's)		
Current:			
Federal	\$3,823	\$4,739	\$4,876
State	634	826	790
Total current income taxes	<u>4,457</u>	<u>5,565</u>	<u>5,666</u>
Deferred:			
Federal			
Accelerated depreciation	688	832	1,138
Rate refunds	--	221	(221)
Unbilled revenues	324	(121)	--
Other	(134)	(287)	(181)
State	236	127	102
Total deferred income taxes	<u>1,114</u>	<u>772</u>	<u>838</u>
Investment tax credits - net:			
Federal	(237)	(239)	(248)
State	95	52	80
Total investment tax credits - net	<u>(142)</u>	<u>(187)</u>	<u>(168)</u>
Total provision included in income taxes	5,429	6,150	6,336
Less - Included in other income or operation expense	<u>(49)</u>	<u>(35)</u>	<u>(5)</u>
Included in operating expenses as taxes - income	5,478	6,185	6,341
Cumulative effect of accounting change			
Federal	464	--	--
State	93	--	--
Total provision for income taxes	<u>\$6,035</u>	<u>\$ 6,185</u>	<u>\$ 6,341</u>

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(6) TAX MATTERS (Continued)

The following is a reconciliation between the computed federal income tax expense (tax rates of 34 per cent in 1989 and 1988, and 43 per cent in 1987, times pre-tax income) and the total provision for federal income tax expenses:

For fiscal years ended September 30,	<u>1989</u>		<u>1988</u>		<u>1987</u>	
	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
	(000's)	of Pre-tax Income	(000's)	of Pre-tax Income	(000's)	of Pre-tax Income
Computed federal income tax expense	\$5,203	34.0	\$5,166	34.0	\$5,524	43.0
Amortization of investment tax credit	(237)	(1.5)	(239)	(1.6)	(248)	(1.9)
Out-of-period items at different tax rates	--	--	233	1.5	53	0.4
Adjustment of deferred taxes	(72)	(0.5)	--	--	--	--
Other, net	34	0.2	(15)	(0.1)	35	0.3
Total provision for federal income taxes	<u>\$4,928</u>	<u>32.2</u>	<u>\$5,145</u>	<u>33.8</u>	<u>\$5,364</u>	<u>41.8</u>

( ) Denotes red figure.

Tax returns for 1980 through 1986 have been audited by the Internal Revenue Service, and tax deficiencies of approximately \$1.5 million have been proposed. Issues are being contested, and the potential impact on net income is not believed to be material, since the issues consist of income tax provision timing differences.

Tax returns for 1988 and 1987 currently are under audit by the Internal Revenue Service.

Illinois income tax returns for 1987 and 1986 currently are under audit by the Illinois Department of Revenue.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(7) DEFERRED CHARGES

	As of September 30,	
	1989	1988
	(000's)	
Debt expense being amortized over the lives of outstanding issues	\$ 257	\$ 292
Energy Conservation Plan expenses	133	119
Interest on gas sales revenue refundable	301	184
IRAPP shortfall amounts	155	96
Payments of charges for pipeline suppliers' take-or-pay costs	--	720
Other	370	147
	<u>\$1,216</u>	<u>\$1,558</u>

(8) REDEEMABLE CUMULATIVE PREFERRED STOCK

	9.0% Series
Year of issue	1980
Shares outstanding	30,000
Involuntary liquidation preference (000's)	\$ 3,000
Annual dividends per share	\$ 9.00
Redemption options:	
Currently effective redemption price per share	(a)
Redemption price per share decreases annually to issue price by (year)	(a)
Redemption through certain refunding operations not permitted prior to (year)	1990

(a) Not currently redeemable at the option of the Company.

(9) COMMON STOCK

No common stock was issued during the fiscal years 1987 through 1989.

(10) SINKING FUND REQUIREMENTS

There are no sinking fund requirements for preferred stock outstanding at September 30, 1989. The preferred stock outstanding at September 30, 1989, is required to be redeemed in its entirety, \$3.0 million, on its redemption date of October 1, 1990.

Sinking fund requirements and maturities of long-term debt outstanding at September 30, 1989, for fiscal years 1990 through 1994 are \$2.2 million for 1990, \$2.4 million for 1991, \$2.5 million for 1992, \$0.5 million for 1993, and \$4.5 million for 1994.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(11) SHORT-TERM BORROWING AND COMPENSATING BALANCES

Short-term cash needs of the Company are met through bank loans and/or the issuance of commercial paper. The outstanding total amount of these borrowings cannot at any time exceed total bank credit then in effect.

To cover projected short-term credit needs of Peoples Gas and to support the long-term status of Peoples Gas' Adjustable-Rate Mortgage Bonds Series W, \$63 million in bank credit through an irrevocable revolving credit agreement with various banks was maintained during the first seven months of fiscal 1989, under which the Company could borrow up to \$15 million.

Effective May 1, 1989, the Company and its affiliate, Peoples Gas, entered into a new irrevocable credit agreement with various banks, providing for maximum credit of \$118 million, of which the Company could borrow up to \$20 million. The agreement will expire on April 30, 1992.

The new agreement increases the credit amount available to Peoples Gas in order to also support the long-term status of the Adjustable-Rate Mortgage Bonds, Series Y and Z.

Payment for the revolving credit agreement with the banks is through compensating balances and/or fees. There are no legal restrictions on withdrawal of compensating balances.

For additional information on short-term borrowings, see Schedule IX.

(12) CAPITAL COMMITMENTS

Total contract and purchase order commitments of the Company at September 30, 1989, amounted to approximately \$1.9 million.

(13) ASSETS SUBJECT TO LIEN

The Indenture of Mortgage, dated April 1, 1955, as supplemented, securing the First and Refunding Mortgage Bonds issued by the Company, constitutes a direct, first-mortgage lien on substantially all property owned by the Company.

(14) EXPLORATION SUBSIDIARY

North Shore Exploration Company, a wholly owned subsidiary of the Company, was formed in 1973 to engage, directly or indirectly, in lease-acquisition, exploration, and development programs. The subsidiary has made investments totaling \$4.1 million and through September 30, 1989, has amortized \$3.9 million. The Company is allowed by the Illinois Commerce Commission to include such investments in its rate base and treat any profits or losses as utility transactions.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(14) EXPLORATION SUBSIDIARY (Continued)

Currently, the exploration company owns small interests in the net profits of leased hydrocarbon-producing offshore blocks through six separate agreements. The exploration company receives monthly distributions of its portion of net profits. In fiscal 1989, these cash distributions totaled \$0.6 million. Amortization of the investment for this same period totaled \$0.1 million. No other business activity occurred during the fiscal year. The last investment in this venture was made in fiscal 1975, and no additional investments are anticipated.

(15) SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

During the fourth quarter of fiscal 1989, the Company changed, effective October 1, 1988, its method of accounting for revenues. (See Note (1)b of Notes to Consolidated Financial Statements.) Data previously reported for the first three quarters of fiscal 1989 have been restated to reflect the newly adopted accounting principle. Per share data are omitted since the Company is a wholly owned subsidiary of Peoples Energy.

Fiscal Quarters	Operating Revenues	Operating Income	Cumulative Effect of Accounting Change	Net Income Applicable to Common Stock
	(000's)			
1989 (as restated)				
First	\$40,333	\$ 5,076	\$ 900	\$ 4,786
Second	60,490	7,422	--	6,256
Third	21,001	1,208	--	434
Fourth	11,810	(379)	--	(1,372)
1989 (as previously reported)				
First	33,928	4,133	--	2,944
Second	61,621	7,633	--	6,467
Third	26,373	1,960	--	1,186
1988 (as reported)				
First	32,767	4,176	--	2,993
Second	57,941	8,383	--	7,161
Third	23,163	2,165	--	1,272
Fourth	9,842	(733)	--	(1,646)
1988 (pro forma)				
First	37,517	5,871	--	3,751
Second	57,059	8,079	--	7,025
Third	18,725	593	--	569
Fourth	9,921	(722)	--	(1,641)

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(16) EVENT (UNAUDITED) SUBSEQUENT TO DATE OF AUDITORS' REPORT--RECOVERY OF  
SUPPLIER CHARGES FOR TAKE-OR-PAY

Reference is made to Note (3) of the Notes to Consolidated Financial Statements.

On December 5, 1989, the Illinois Appellate Court issued an opinion reversing and remanding to the Commission the Commission's November 22, 1988 order which allowed state gas utilities, including the Company, to fully recover separate supplier charges for take-or-pay, through the Uniform Gas Charge, from all classes of customers. The Court, with one of three judges dissenting, held that, contrary to the finding of the Commission, the Commission is not precluded by the federal preemption and filed rate doctrines from requiring gas utilities to absorb a portion of take-or-pay charges imposed by pipeline suppliers pursuant to the policy of the FERC's Order No. 500. The Court explicitly refrained, however, from offering any opinion as to whether any of such charges should be absorbed by utilities, leaving that determination to the Commission on remand, after taking evidence. Under applicable Court rules, the Court's mandate effectuating its opinion will not issue until after the disposition of all requests for rehearing and any subsequent appeals to the Illinois Supreme Court. The Company believes that the Court's opinion is erroneous as a matter of law and intends to contest it by seeking rehearing or appeal or both. While the Company cannot predict the final outcome on appeal, the Company believes that the Commission's decision is fully supported by statute and precedent, federal and state, and the evidentiary record and, accordingly, will ultimately be upheld on appeal.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING  
AND FINANCIAL DISCLOSURE

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY

IDENTIFICATION OF DIRECTORS

<u>Name, Principal Occupation, and Other Directorships</u>	<u>Age at 11-30-89</u>	<u>Company Directorship Since</u>
J. Bruce Hasch Executive Vice President of the Company, Peoples Energy, and Peoples Gas; Director of Peoples Energy and Peoples Gas.	51	1986
James Hinchliff Senior Vice President and General Counsel of the Company, Peoples Energy, and Peoples Gas; Director of Peoples Gas.	49	1985
Michael S. Reeves Executive Vice President of the Company, Peoples Energy, and Peoples Gas; Director of Peoples Gas.	54	1988
Richard E. Terry President and Chief Operating Officer of the Company, Peoples Energy, and Peoples Gas; Director of Peoples Energy and Peoples Gas.	52	1982
Eugene A. Tracy Chairman of the Board and Chief Executive Officer of the Company, Peoples Energy, and Peoples Gas; Director of LaSalle National Bank.	61	1978

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY (Continued)

IDENTIFICATION OF EXECUTIVE OFFICERS

	<u>Position at November 30, 1989</u>	<u>Age at 11-30-89</u>	<u>Position Held Since</u>
Frank H. Blackmore	Vice President	54	1989
Emmet P. Cassidy	Secretary and Treasurer	56	1989
Patrick J. Doyle	Vice President	52	1985
J. Bruce Hasch	Executive Vice President	51	1985
George G. Henning	Vice President and Controller	62	1989
James Hinchliff	Senior Vice President and General Counsel	49	1989
John A. Lawrisuk	Vice President	61	1981
John E. McManus	Vice President	60	1989
John F. Mooney	Vice President	55	1987
Thomas M. Patrick	Vice President and Deputy General Counsel	43	1989
James D. Pitts, Jr.	Vice President	51	1989
Michael S. Reeves	Executive Vice President	54	1987
Richard E. Terry	President and Chief Operating Officer	52	1987
Eugene A. Tracy	Chairman of the Board and Chief Executive Officer	61	1981

Directors and executive officers of the Company were elected to serve for a term of one year or until their successors are duly elected and qualified.

There are no family relationships among directors and executive officers of the Company.

All of the directors and executive officers of the Company have been continuously employed by the Company and/or its affiliates in various capacities for at least 10 years.



## ITEM 11. EXECUTIVE COMPENSATION

The executive officers of the Company serve both the Company and its affiliate, Peoples Gas. Remuneration is paid by Peoples Gas with appropriate amounts billed to the Company for the time such officers serve North Shore. The Company was billed \$404,396 for the services of these officers during fiscal 1989, including approximately \$73,000 for the services of Mr. Tracy. No other executive officer's cash remuneration for service to North Shore exceeded \$60,000. Information regarding executive compensation paid by Peoples Gas and its affiliates to Peoples Gas officers is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1989.

### Compensation of Directors

All directors of the Company were officers of the Company who received no compensation for serving as directors.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

### SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

As of November 30, 1989, voting securities of the Company were beneficially owned as follows:

<u>Name and Address</u>	<u>Number of Shares Owned</u>	<u>Per Cent of Class</u>
<u>Common Stock without par value</u>		
Peoples Energy Corporation 122 South Michigan Avenue Chicago, Illinois 60603	<u>3,625,887</u>	<u>100%</u>
<u>Redeemable Cumulative Preferred Stock, \$100 Par Value</u>		
GMAC Commercial Corporation General Motors Building 3044 West Grand Boulevard Detroit, Michigan 48202	<u>30,000</u>	<u>100%</u>

### SECURITY OWNERSHIP OF MANAGEMENT

No equity securities of the Company are beneficially owned directly or indirectly by any director or officer of the Company.

Information regarding common stock, without par value, of Peoples Energy beneficially owned directly or indirectly by directors and executive officers of the Company is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1989.

### CHANGES IN CONTROL

None.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

None.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES, AND REPORTS ON FORM 8-K

(a) 1. Financial Statements: Page  
See Part II, Item 8. 12

2. Financial Statement Schedules:

Schedule  
Number

V	Property, Plant and Equipment, at Original Cost	37
VI	Accumulated Provision for Depreciation of Property, Plant and Equipment	39
VIII	Valuation and Qualifying Accounts	41
IX	Short-Term Borrowings	42
X	Supplementary Income Statement Information	43

3. Exhibits:

See Exhibit Index on page 45.

(b) Reports on Form 8-K filed during the final quarter of fiscal year 1989:

None.

North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 1 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<u>Fiscal Year Ended September 30, 1989</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,966	\$ 47	\$ --	\$ --	\$ 4,013
Storage plant	7,484	221	--	--	7,705
Distribution plant	137,436	14,178	594	(431)	150,589
General plant	8,392	1,557	883	--	9,066
Construction work in progress	5,982	(2,314)	--	--	3,668
Gas stored underground - non-current	<u>725</u>	<u>25</u>	<u>--</u>	<u>--</u>	<u>750</u>
Total public utility facilities	163,985	13,714	1,477	(431) (d)	175,791
Non-utility property	<u>--</u>	<u>--</u>	<u>--</u>	<u>431</u>	<u>431</u>
Total property, plant and equipment, at original cost	<u>\$163,985</u>	<u>\$ 13,714</u>	<u>\$ 1,477 (a)</u>	<u>\$ --</u>	<u>\$176,222</u>
<u>Fiscal Year Ended September 30, 1988</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,850	\$ 133	\$ 17	\$ --	\$ 3,966
Storage plant	7,484	--	--	--	7,484
Distribution plant	129,910	8,211	685	--	137,436
General plant	7,980	889	477	--	8,392
Construction work in progress	1,071	4,911	--	--	5,982
Gas stored underground - non-current	<u>725</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>725</u>
Total public utility facilities	151,020	14,144	1,179	--	163,985
Non-utility property	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>
Total property, plant and equipment, at original cost	<u>\$151,020</u>	<u>\$ 14,144</u>	<u>\$ 1,179 (a)</u>	<u>\$ --</u>	<u>\$163,985</u>

**PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST**  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<b><u>Fiscal Year Ended September 30, 1987</u></b>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,843	\$ 18	\$ 1	\$ (10)	\$ 3,850
Storage plant	7,271	213	--	--	7,484
Distribution plant	116,828	13,547	666	201	129,910
General plant	7,936	1,057	812 (b)	(201)	7,980
Construction work in progress	1,392	(321)	--	--	1,071
Gas stored underground - non-current	<u>701</u>	<u>24</u>	<u>--</u>	<u>--</u>	<u>725</u>
Total public utility facilities	137,971	14,538	1,479	(10) (c)	151,020
Non-utility property	<u>630</u>	<u>--</u>	<u>640</u>	<u>10</u>	<u>--</u>
Total property, plant and equipment, at original cost	<u>\$138,601</u>	<u>\$ 14,538</u>	<u>\$ 2,119 (a)</u>	<u>\$ --</u>	<u>\$151,020</u>

( ) Denotes red figure.

Notes: (a) Represents:

Retirements charged to accumulated provision for depreciation Schedule (VI)  
Cost of land retired at Peterson Road

<u>1989</u>	<u>1988</u>	<u>1987</u>
\$1,477	\$1,179	\$1,479
--	--	640
<u>\$1,477</u>	<u>\$1,179</u>	<u>\$2,119</u>

(b) Includes \$261 thousand applicable to a change in minimum capitalization from \$250 to \$500.

(c) Represents the transfer of Peterson Road land to non-utility property.

(d) Represents the transfer of Deerfield Plant property to non-utility property.

North Shore Gas Company and Subsidiary Companies

ACCUMULATED PROVISION FOR DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

(000's)

Column A	Column B	Column C	Column D	Column E	Column F
Description	Balance at beginning of period	Additions charged to cost and expenses	Retirement of property at cost	Other changes	Balance at end of period
		Depreciation expense	Clearing accounts		
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 2,366	\$ 122	\$ --	\$ --	\$ 2,490
Storage plant	2,311	259	--	--	2,570
Distribution plant	45,023	4,519	594	(11)	48,511
General plant	2,071	181	803	(122)	2,700
Total public utility facilities	52,573	5,081	1,477	(123)	56,271
Non-utility property	--	--	--	--	287
Total accumulation provision for depreciation	52,573	5,081	1,477	(123)	56,271
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 2,261	\$ 125	\$ --	\$ --	\$ 2,386
Storage plant	2,068	253	--	--	2,311
Distribution plant	41,636	4,253	604	(11)	45,023
General plant	2,685	177	477	(87)	2,871
Total accumulation provision for depreciation	48,650	4,808	1,178	(98)	52,573

Fiscal Year Ended September 30, 1999

North Shore Gas Company and Subsidiary Companies

ACCUMULATED PROVISION FOR DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

(000's)

Column A	Column B	Column C		Column D			Column E	Column F
Description	Balance at beginning of period	Additions charged to costs and expenses (a)		Deduct retirements			Other changes	Balance at end of period
		Depreciation expense	Clearing accounts	Retirement of property at cost	Cost of dismantling	Stores and miscellaneous (salvage)		
Fiscal Year Ended September 30, 1987								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 2,132	\$ 130	\$ --	\$ 1	\$ --	\$ --	\$ --	\$ 2,261
Storage plant	1,805	253	--	--	--	--	--	2,058
Distribution plant	38,487	3,934	--	666	198	(2)	77	41,636
General plant	2,875	224	389	812 (b)	--	(73)	(64)	2,685
Total accumulation provision for depreciation	\$45,299	\$ 4,541	\$ 389	\$ 1,479	\$ 198	\$ (75)	\$ 13 (c)	\$48,640

( ) Denotes red figure.

Notes: (a) See Note (1)e of Notes to Consolidated Financial Statements  
with respect to the basis for the provision for depreciation.

(b) Includes \$261 thousand applicable to a change in minimum capitalization  
from \$250 to \$500.

(c) Represents the following:

	1989	1987
Accumulated provision for depreciation applicable to property acquired	\$ 4	\$ 2
Proceeds from sale of property	14	11
Capitalized depreciation transferred	16	--
Transfer of Deerfield's accumulated provision for depreciation to non-utility property	(287)	--
	<u>\$ (253)</u>	<u>\$ 13</u>

North Shore Gas Company and Subsidiary Companies

Schedule VIII

VALUATION AND QUALIFYING ACCOUNTS  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance at beginning of period</u>	<u>Additions Charged to costs and expenses</u>	<u>Deductions</u> <u>Charges for the purpose for which the reserves or deferred credits were created</u>	<u>Balance at end of period</u>
<u>For Fiscal Year Ended September 30, 1989</u>				
RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 646</u>	<u>\$ 691</u>	<u>\$ 717</u>	<u>\$ 620</u>
<u>For Fiscal Year Ended September 30, 1988</u>				
RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 544</u>	<u>\$ 842</u>	<u>\$ 740</u>	<u>\$ 646</u>
<u>For Fiscal Year Ended September 30, 1987</u>				
RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 634</u>	<u>\$ 903</u>	<u>\$ 993</u>	<u>\$ 544</u>

North Shore Gas Company and Subsidiary CompaniesSHORT-TERM BORROWINGS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E (a)</u>	<u>Column F (b)</u>
<u>Category of Aggregate</u> <u>Short-Term Borrowings</u>	<u>Balance at</u> <u>End of Period</u>	<u>Weighted Average</u> <u>Interest Rate</u> <u>End of Period</u>	<u>Maximum Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Average Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Weighted Average</u> <u>Interest Rate</u> <u>During the Period</u>
<u>Fiscal Year Ended September 30, 1989</u>					
Commercial Paper	\$ 5,000	8.68%	\$ 6,000	\$ 1,500	8.74%
<u>Fiscal Year Ended September 30, 1988</u>					
Commercial Paper	\$ --	--	\$13,500	\$ 1,967	7.18%
<u>Fiscal Year Ended September 30, 1987</u>					
Commercial Paper	\$11,500	7.28%	\$11,500	\$ 1,703	6.97%

(a) Computed by multiplying the amounts outstanding by the days outstanding and dividing the results by the number of days used.

(b) Computed by dividing the applicable interest expense by the average amount outstanding during the period.



North Shore Gas Company and Subsidiary Companies

..

SUPPLEMENTARY INCOME STATEMENT INFORMATION

Maintenance, depreciation, royalties, advertising costs, and research and development costs, other than those specifically disclosed in the Consolidated Statements of Income, are not significant.

Significant taxes, other than taxes on income, including those charged to clearing and other accounts, are summarized as follows:

	Fiscal Years Ended September 30,		
	<u>1989</u>	<u>1988</u> (000's)	<u>1987</u>
Real estate, invested capital, personal property, and state franchise	\$ 1,290	\$ 1,008	\$ 945
Illinois public utility	5,600	5,098	5,322
Municipal public utility	2,779	2,633	3,176
Social security	690	649	712
Other	<u>397</u>	<u>314</u>	<u>308</u>
Total	<u>\$10.756</u>	<u>\$ 9.702</u>	<u>\$10.463</u>

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NORTH SHORE GAS COMPANY

Date: December 26, 1989

By: E. A. TRACY  
E. A. Tracy  
Chairman of the Board and Chief  
Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on December 26, 1989.

E. A. TRACY  
E. A. Tracy

Chairman of the Board and Chief Executive  
Officer and Director  
(Principal Executive Officer)

J. B. HASCH  
J. B. Hasch

Executive Vice President and Director  
(Principal Financial Officer)

G. G. HENNING  
G. G. Henning

Vice President and Controller  
(Principal Accounting Officer)

JAMES HINCHLIFF  
James Hinchliff

Director

MICHAEL S. REEVES  
Michael S. Reeves

Director

RICHARD E. TERRY  
Richard E. Terry

Director

North Shore Gas Company and Subsidiary Companies

EXHIBIT INDEX

- (a) The exhibits listed below are filed herewith and made a part thereof:

<u>Exhibit Number</u>	<u>Description of Document</u>	<u>Page Number</u>
3-a	Amendment to the By-Laws of the Registrant, dated July 5, 1989.	46
3-b	By-Laws, as last amended, dated July 5, 1989.	47
18	Arthur Andersen & Co. preferability letter regarding change in method of accounting for revenues, effective October 1, 1988.	67

- (b) Exhibits listed below have been filed heretofore with the Securities and Exchange Commission pursuant to the Securities Act of 1933, as amended, and/or the Securities Exchange Act of 1934, as amended, and are incorporated herein by reference. The file number and exhibit number of each such exhibit are stated in the description of such exhibits.

<u>Exhibit Number</u>	<u>Description of Document</u>
3-c	Articles of Incorporation of the Registrant as amended on April 13, 1987 (Registrant Form 10-K for fiscal year ended September 30, 1987, Exhibit 3-b).
4-a	Indenture, dated as of April 1, 1955, from the Company to Continental Illinois National Bank and Trust Company of Chicago as Trustee; Third Supplemental Indenture, dated as of December 20, 1963 (North Shore-File No. 2-35965, Exhibit 4-1); Fifth Supplemental Indenture, dated as of February 1, 1970 (File No. 2-35965, Exhibit 4-2); Sixth Supplemental Indenture, dated as of October 1, 1973 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-3); Seventh Supplemental Indenture, dated as of February 15, 1977 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-4); Eighth Supplemental Indenture, dated as of September 15, 1980 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-5); and Ninth Supplement Indenture, dated as of December 1, 1987 (Form 10-K for the fiscal year ended September 30, 1987, Exhibit 4).

---

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM 10-K**

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 1988      Commission File Number 2-35965

**NORTH SHORE GAS COMPANY**

(Exact name of registrant as specified in its charter)

**Illinois**

(State or other jurisdiction of  
incorporation or organization)

**38-1558720**

(IRS Employer  
Identification No.)

**122 South Michigan Avenue, Chicago, Illinois**

(Address of principal executive offices)

**60603**

(Zip Code)

**Registrant's telephone number, including area code:**

**(312) 431-4000**

**Securities registered pursuant to Section 12(b) of the Act:   None**

**Securities registered pursuant to Section 12(g) of the Act:   None**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No   

State the aggregate market value of the voting stock held by non-affiliates of the registrant:

Redeemable Cumulative Preferred Stock, \$3,000,000 at November 30, 1988, based on the price at which the stock was sold.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, without par value, 3,625,887 shares outstanding at November 30, 1988.

Documents Incorporated by Reference  
None

---

## CONTENTS

<u>Item No.</u>		<u>Page No.</u>
	<u>Part I</u>	
1.	Business	3
2.	Properties	8
3.	Legal Proceedings	8
4.	Submission of Matters to a Vote of Security Holders	8
	<u>Part II</u>	
5.	Market for the Company's Common Stock and Related Stockholder Matters	9
6.	Selected Financial Data	9
7.	Management's Discussion and Analysis of Results of Operations and Financial Condition	10
8.	Financial Statements and Supplementary Data	13
9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	30
	<u>Part III</u>	
10.	Directors and Executive Officers of the Company	31
11.	Executive Compensation	33
12.	Security Ownership of Certain Beneficial Owners and Management	33
13.	Certain Relationships and Related Transactions	33
	<u>Part IV</u>	
14.	Exhibits, Financial Statement Schedules and Reports on Form 8-K	34
	Signatures	42
	Exhibit Index	43

North Shore Gas Company

ANNUAL REPORT ON FORM 10-K

FISCAL YEAR ENDED SEPTEMBER 30, 1988

PART I

ITEM 1. BUSINESS

GENERAL

North Shore Gas Company (Company) is an operating public utility engaged primarily in the purchase, storage, distribution, sale and transportation of natural gas at retail to more than 110,000 residential, commercial and industrial customers within its service area of approximately 275 square miles, located in northeastern Illinois. It serves 56 communities and adjacent areas, including those situated along Lake Michigan from Winnetka, Illinois to the Illinois-Wisconsin state line. This area, with an estimated population of 490,000, contains residential concentrations and a diversity of industrial and commercial establishments, as well as some farm lands. The Company had 237 employees at September 30, 1988.

The Company holds certificates of public convenience and necessity issued by the Illinois Commerce Commission (Commission) for the conduct by the Company of its operations in the territory which it serves. It holds a license agreement from Lake County, Illinois, and, with minor exceptions, franchises from all of the incorporated cities and villages in its service territory. The franchises are of various terms and expiration dates, and are generally subject to various other conditions, restrictions or limitations not deemed materially burdensome.

At September 30, 1988, the common stock of the Company and of its affiliate, The Peoples Gas Light and Coke Company (Peoples Gas), was wholly-owned by Peoples Energy Corporation (Peoples Energy).

COMPETITION

Competition in varying degrees exists between natural gas and other fuels or forms of energy available to consumers in the Company's service area. Natural gas prices declined during the last year enabling gas to maintain a lower price than competing energies. Overall, natural gas prices in the Company's service area compared very favorably on a national basis.

A number of the customers of the Company are substituting customer-owned gas for gas purchases from the Company, utilizing the availability of pipeline transportation as well as the Company's own transportation service. Under existing rates, the Company experiences no loss of distribution margin due to customer shifts from gas service to transportation service. The Company has utilized the increased availability of transportation to make purchases in the competitive spot market, thereby reducing the average cost of gas that must be recovered from customers.

Despite the access to spot market supplies afforded by open-access transportation, the Company is concerned because it is not known how the changing use of pipeline services under the new open-access rules will affect the security and reliability of long-term supplies from pipelines for distributors.

## ITEM 1. BUSINESS (Continued)

### COMPETITION (Continued)

A pipeline may seek to provide transportation service directly to end-users. Such direct service by a pipeline to an end-user would bypass the local distributor's service and reduce its earnings. However, to the best of the Company's knowledge, no such service has been proposed for any customers of the Company.

### SALES AND RATES

The Company sells natural gas having an average heating value of approximately 1,000 British thermal units (Btu's) per cubic foot.\* Sales are made and service rendered by the Company pursuant to a rate schedule on file with the Illinois Commerce Commission (Commission) containing various service classifications largely reflecting customers' different uses and size of consumption. Monthly adjustments to the Gas Charge under the Company's rate schedule provide for the pass-through of increases or decreases in natural gas supplier rates, purchased storage service costs, transportation charges, liquefied petroleum gas costs and purchases of synthetic natural gas (SNG). In addition, under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or a current asset (with a contra entry to gas costs), and the fiscal year-end balance is amortized over the 12-month period beginning the following January 1.

The business of the Company is seasonal because a large element of the Company's customer load consists of space heating. For a discussion as to the effect of the seasonal nature of gas sales upon net income and cash flow, see "Results of Operations" and "Liquidity and Capital Resources" in Management's Discussion and Analysis of Results of Operations and Financial Condition.

The basic marketing plan of the Company is to retain its strong position in the residential, commercial and industrial markets while seeking dominant market share in new construction and expansion of the commercial and industrial markets. The Company will also pursue non-traditional markets such as gas air cooling, cogeneration and the use of compressed natural gas for fueling buses and vehicles.

### STATE LEGISLATION AND REGULATION

The Company is subject to the jurisdiction of and regulation by the Illinois Commerce Commission (Commission), which has general supervisory and regulatory powers over practically all phases of the public utility business in Illinois, including rates and charges, issuance of securities, services and facilities, systems of accounts, investments, safety standards, transactions with affiliated interests, as defined in the Illinois Public Utilities Act, and other matters.

---

\* All volumes of natural gas set forth in this report are stated on a 1,000 Btu (per cubic foot) billing basis.

## ITEM 1. BUSINESS (Continued)

### STATE LEGISLATION AND REGULATION (Continued)

Under the Illinois Residential Affordable Payment Program (IRAPP), the Company is prohibited from discontinuing gas service to any participating customer who pays the monthly obligation required by IRAPP. See Note (1)1 of Notes to Consolidated Financial Statements.

The statutory authority authorizing IRAPP expires on December 31, 1988. The Company and other utilities have agreed to continue IRAPP pending action by the Illinois legislature to reauthorize IRAPP, which is anticipated to occur in early 1989.

### FEDERAL LEGISLATION AND REGULATION

By Order entered on December 6, 1968 (Holding Company Act Release No. 16233), the Securities and Exchange Commission (SEC), pursuant to Section 3(a)(1) of the Public Utility Holding Company Act of 1935 (Act) exempted Peoples Energy and its subsidiary companies as such (including the Company) from the provisions of the Act other than Section 9(a)(2) thereof.

In late 1985, and early 1986, the Federal Energy Regulatory Commission (FERC) issued Order Nos. 436 and 436-A through E which, among other things, offered pipelines an option to transport gas on an "open-access" nondiscriminatory basis for all shippers under expedited regulatory procedures. Pipelines that elected this option were required, as a condition thereto, to allow firm sales customers to reduce their gas purchase demand volumes under firm sales contracts or convert such purchase demand volumes to firm transportation service by up to 100 per cent over a five-year period following the pipeline's election.

In June 1987, the D.C. Circuit Court of Appeals determined that the 436 series of orders should be vacated and remanded to the FERC for further consideration. In response to the Court's decision, the FERC issued Order No. 500 which readopts on an interim basis the regulations promulgated by Order No. 436 with certain modifications. The principal modifications to the Order No. 436 regulations adopted in Order No. 500 are: (1) a requirement that producers grant take-or-pay credits to pipelines transporting their gas; (2) a policy as to the acceptable mechanism for the passthrough to pipeline customers of take-or-pay buyout and buydown costs; (3) principles upon which pipelines may charge customers for the cost of holding gas supplies to serve them; and (4) elimination of the pipeline customer's option to reduce contract demand. Order No. 500 has been appealed to a Federal court of appeal.

In December 1986, the FERC voted to deny rehearing of Order No. 451, which raised the ceiling prices permitted to be paid for all categories of "old" gas, still regulated under the Natural Gas Policy Act (NGPA), to that of the highest-priced old gas category. The order also established a "good faith negotiation" procedure by which producers of such gas may seek increased prices up to the new ceiling. A portion of contracted gas reserves of the pipeline suppliers for the Company is subject to this rule. At this time, the Company cannot determine the ultimate impact on customers gas bills of Order No. 451, which is under appeal to a Federal court of appeal.

In March 1988, the Company's principal supplier, Natural Gas Pipeline Company of America (Natural), filed with the FERC a revised plan for a gas supply charge. This inventory fee would compensate Natural for holding gas supplies to meet the purchase entitlements of its utility customers, including the Company. Under Natural's proposal, a volumetric charge would be levied on quantities reserved but not taken by a customer in any month.



## ITEM 1. BUSINESS (Continued)

### FEDERAL LEGISLATION AND REGULATION (Continued)

As the Company disagreed with specific terms of Natural's filing, it, along with Natural's other major customers, subsequently filed a counterproposal. This customer alternative was geared to meet the customers' requirements for flexibility in their choice of monthly entitlements and in their level of discretionary purchases. Following negotiations, the pipeline and customer group filed a joint settlement which provides for a volumetric deficiency charge to be levied on a portion of volumes reserved but not taken. The joint settlement also provides for winter and summer price caps on Natural's commodity rates, flexibility in customer nominations and a one-time opportunity to decrease existing daily contract demand entitlements by up to 15%. The FERC approved the joint settlement on July 29, 1988, subject to certain conditions. On rehearing of its July 29, 1988 approval order, the FERC approved immediate implementation of the one-time daily contract demand reductions. In December, Natural elected not to accept the joint settlement.

On July 1, Natural petitioned the FERC for a rate increase, of which approximately \$4 million would be passed on to the Company. The request was part of a filing that also proposes Natural's introduction of seasonal rates. Under this plan, rates for delivery of gas to the pipeline's customers would be significantly higher from November through March than from April through October. The parties have entered into settlement discussions.

### GAS SUPPLY ADVANCES AND INVESTMENTS

During the natural gas shortage of the 1970's, the Company undertook several programs to augment its gas supply. From 1973 through 1975, the Company, with Commission approval, made equity investments in development ventures. At September 30, 1988, \$430,000 in equity investments remain outstanding. The Company is allowed by the Commission to include such investments in its rate base and treat any profits or losses as utility transactions. See Note (13) of Notes to Consolidated Financial Statements for information on the Company's exploration subsidiary.

On June 2, 1988, the Company completed a settlement involving advance payments made in 1977 for gas supply exploration. Under the settlement, the Company was repaid \$790,000 in principal and \$340,000 in interest.

### CURRENT GAS SUPPLY

The following tabulation shows the expected peak-day availability of gas in thousand cubic feet (Mcf) during the 1988-89 heating season:

<u>Source</u>	<u>Peak-Day Availability (Mcf)</u>	<u>Year of Contract Expiration</u>
Flow Gas		
Natural.....	135,371	1990 (a)
Company (LP).....	60,000	
	<u>195,371</u>	
Storage Gas		
Natural.....	97,153 (b)	1990-1995 (a)
Peoples Gas (Manlove).....	63,809 (c)	1990
	<u>160,962</u>	
Total expected peak-day availability....	<u>356,333</u> (d)	

ITEM 1. BUSINESS (Continued)

CURRENT GAS SUPPLY (Continued)

- (a) Natural Gas Pipeline Company of America (Natural) may not terminate service at the expiration of service agreements without receiving prior authorization from the Federal Energy Regulatory Commission (FERC).
- (b) The Company has storage service withdrawals available from Natural of (1) 53,029 Mcf per day subject to maximum seasonal withdrawal of 30 times the maximum daily withdrawal under a service agreement extending to 1990, (2) 6,657 Mcf per day under a service agreement extending to 1992, (3) 4,055 Mcf per day in the peak month, which is January, under a service agreement extending to 1991, (4) 3,412 Mcf per day under a service agreement extending to 1995, and (5) 30,000 Mcf per day under a service agreement expiring in 1990.
- (c) The Company has a gas storage agreement with Peoples Gas which provides a maximum withdrawal of 63,809 Mcf of storage service per day. The agreement also makes available additional quantities, if available, equal to its pro rata share.
- (d) See discussion of Order No. 436 and Order No. 500 under "Federal Legislation and Regulation".

The Company's sources of gas supply (including gas transported for customers) in million cubic feet (MMcf) for the three fiscal years ended September 30, 1988, 1987 and 1986 were as follows:

	<u>1988</u>	<u>1987</u>	<u>1986</u>
Source:			
Natural (a)	18,315	11,330	31,625
Other Suppliers (a)	9,173	15,470	918
Peoples Gas - SNG (b)	--	--	276
- Other	--	--	944
Liquefied Petroleum Gas Produced	12	5	3
Customer Owned Gas - Received	7,045	4,390	17
Underground Storage - Net	(247)	255	(559)
Company Use, Franchise Requirements and Unaccounted for Gas	<u>(337)</u>	<u>(287)</u>	<u>(148)</u>
Total (c)	<u>33,961</u>	<u>31,163</u>	<u>33,076</u>

( ) Denotes red figure.

- (a) The Company began making significant purchases of supplies in the competitive spot market in fiscal 1987, substituting these supplies for more expensive pipeline supplies. Such purchases are made on a month-to-month basis whenever they produce a savings in gas costs without jeopardizing supply security and reliability. See discussion of Order No. 436 and Order No. 500 under "Federal Legislation and Regulation".
- (b) North Shore's service agreement with Peoples Gas, which provided for the purchase of 10 per cent of the production of Peoples Gas' synthetic natural gas (SNG) plant, expired in fiscal 1986 and was not renewed.
- (c) The variation in total supply from year-to-year is due primarily to weather.

## ITEM 2. PROPERTIES

All of the principal plants and properties of the Company have been maintained in the ordinary course of business and are believed to be in satisfactory operating condition. The following is a brief description of the principal plants and operating units of the Company.

The distribution system of the Company, as of September 30, 1988, consisted of 1,752 miles of distribution mains and necessary pressure regulators, approximately 102,000 services (pipe connecting the mains with piping on the customers' premises) and approximately 113,000 meters installed on customers' premises. The Company has liquefied petroleum gasification and storage facilities. It also owns and has a substantial investment in office and service buildings, garages, repair shops and motor vehicles, together with the equipment, tools and fixtures necessary to conduct its business.

Most of the principal plants and properties of the Company, other than mains, services, meters, regulators and cushion gas in underground storage, are located on property owned in fee. Substantially all gas mains are installed in public streets, alleys and highways, or under property owned by others under grants of easements. Meters and house regulators in use and a portion of services are located on premises being served.

Substantially all of the physical properties now owned or hereafter acquired by the Company are subject to (a) the direct, first mortgage lien of the Company's Mortgage to the Continental Illinois National Bank and Trust Company of Chicago, Trustee, to secure the principal amount of the Company's outstanding First Mortgage Bonds and (b) in certain cases, other exceptions and defects which do not interfere with the use of the property.

## ITEM 3. LEGAL PROCEEDINGS

There are no material legal proceedings pending to which the Company is a party.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

## PART II

### ITEM 5. MARKET FOR THE COMPANY'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The Company is a wholly-owned subsidiary of Peoples Energy.

### ITEM 6. SELECTED FINANCIAL DATA

For fiscal years ended September 30,	1988	1987	1986	1985	1984
<b>OPERATING RESULTS (thousands)</b>					
Operating Revenues:					
Residential	\$ 84,320	\$ 81,450	\$ 96,265	\$ 99,472	\$ 98,818
Commercial	27,546	31,229	38,133	40,837	40,319
Industrial	6,017	12,164	30,409	34,052	32,765
Transportation of customer-owned gas	4,990	2,523	7	--	--
Other	840	792	944	966	1,199
Total Operating Revenues	<u>123,713</u>	<u>128,158</u>	<u>165,758</u>	<u>175,327</u>	<u>173,101</u>
Less - Gas costs	71,708	77,616	108,893	118,789	122,314
- Revenue taxes	7,828	8,591	11,094	12,026	11,598
Net Operating Revenues	<u>\$ 44,177</u>	<u>\$ 41,951</u>	<u>\$ 45,771</u>	<u>\$ 44,512</u>	<u>\$ 39,189</u>
Net Income Applicable to Common Stock	\$ 9,780	\$ 7,183	\$ 8,900	\$ 8,782	\$ 6,847
<b>GAS SOLD AND TRANSPORTED (million cubic feet)</b>					
Residential	18,640	16,670	18,161	17,209	18,323
Commercial	6,870	7,288	8,090	7,946	8,377
Industrial	1,478	2,956	6,806	6,867	6,924
Transportation of customer-owned gas	6,973	4,249	19	--	--
Total	<u>33,961</u>	<u>31,163</u>	<u>33,076</u>	<u>32,022</u>	<u>33,624</u>
<b>NUMBER OF CUSTOMERS (average)</b>					
Residential	102,906	99,537	96,281	94,393	93,126
Commercial	6,245	6,241	5,962	5,769	5,595
Industrial	713	704	717	700	695
Transportation	437	52	1	--	--
Total	<u>110,301</u>	<u>106,534</u>	<u>102,961</u>	<u>100,862</u>	<u>99,416</u>
DEGREE DAYS	6,436	5,760	6,747	6,650	7,177
Per cent of normal (6,455)	100	89	105	103	111
<b>ASSETS (thousands)</b>					
Property, plant and equipment	\$163,985	\$151,020	\$138,601	\$128,767	\$121,629
Less-Accumulated depreciation	52,573	48,640	45,299	41,803	38,477
Net Property, Plant and Equipment	<u>\$111,412</u>	<u>\$102,380</u>	<u>\$ 93,302</u>	<u>\$ 86,964</u>	<u>\$ 83,152</u>
Capital expenditures - construction	\$ 14,144	\$ 14,539	\$ 10,810	\$ 8,072	\$ 6,186
Total Assets	<u>\$142,442</u>	<u>\$131,802</u>	<u>\$123,957</u>	<u>\$130,756</u>	<u>\$122,780</u>
<b>CAPITALIZATION AT YEAR-END (thousands)</b>					
Common equity	\$ 54,042	\$ 47,961	\$ 44,295	\$ 41,197	\$ 39,086
Preferred stock	3,000	3,000	3,000	4,000	5,000
Long-term debt	39,345	23,525	27,625	33,082	38,494
Total	<u>\$ 96,387</u>	<u>\$ 74,486</u>	<u>\$ 74,920</u>	<u>\$ 78,279</u>	<u>\$ 82,580</u>
<b>CAPITALIZATION RATIOS AT YEAR-END (per cent)</b>					
Common equity	56	64	59	53	47
Preferred stock	3	4	4	5	6
Long-term debt	41	32	37	42	47
Total	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>

The Company is a wholly-owned subsidiary of Peoples Energy; therefore, cash dividends declared per share and earnings per share are omitted.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Results of Operations

The Company has experienced significant decreases in gross revenues during the past few years. The major factors contributing to these decreases are the direct purchase of gas by some of the Company's customers from producers and brokers rather than from the Company, and a reduction in the unit cost of gas. Neither of these factors has a direct effect on net income. With direct customer purchase of gas, the Company still transports customer-owned gas to end users and recovers profit margins similar to those from conventional gas sales. With respect to reduced gas costs, net income is not directly affected because the Company's tariffs provide for dollar-for-dollar recovery of gas costs. Because these reduced revenue levels do not directly affect net income, the discussion below pertains to "net operating revenues", which the Company considers a more pertinent measure of operating results than gross revenues.

Weather variations affect the volumes of gas delivered for heating and, therefore, can have a significant impact on net income. Net income is not directly affected by the major operating cost - that of gas purchased - because this cost is recovered from retail customers through the gas charge provision in the Company's rate schedule. See Note (1)g of Notes to Consolidated Financial Statements.

Since the Company's properties are reported and recovered through rates at historical costs, the potentially material effect of inflation and changing prices is not reflected in the financial statements.

Net income applicable to common stock increased by \$2.6 million in 1988, primarily due to increased gas deliveries significantly influenced by weather that was relatively normal compared to very warm weather in the previous year, and a lower federal income tax rate as a result of the Tax Reform Act of 1986. The net income effect of these factors was tempered by a refund and a rate reduction. See Note (3) of Notes to Consolidated Financial Statements. The decrease in 1987 was primarily the result of much warmer weather than in 1986. The effect on income of weather in 1987 was mitigated by decreased pension expense principally due to the adoption of new accounting rules under Statement of Financial Accounting Standards No. 87. See Note (4) of Notes to Consolidated Financial Statements.

A summary of significant variations in income is presented below, with explanations following:

(Thousands of dollars)	Fiscal 1988 Over 1987		Fiscal 1987 Over 1986	
	Amount	%	Amount	%
Net operating revenues*	\$2,226	5.3	\$(3,820)	(8.3)
Operation and maintenance expenses	(991)	(5.3)	(100)	(0.5)
Income taxes	(156)	(2.5)	(2,448)	(27.9)
Other income	543	92.3	(836)	(58.7)
Income deductions	1,056	26.3	(609)	(13.2)
Net Income Applicable to Common Stock	2,597	36.2	(1,717)	(19.3)

( ) Denotes red figure.

\* Operating revenues net of gas costs and revenue taxes.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Results of Operations (Continued)

The primary reasons for the increase in 1988 net operating revenues were relatively normal weather in 1988 compared to a very warm 1987, and increased customer demand. The decrease in 1987 resulted mainly from warmer weather.

In 1988, operation and maintenance expenses decreased mainly due to a favorable settlement involving advance payments for gas supply exploration.

Income taxes were down slightly in 1988 as a result of the lower federal income tax rate, which was substantially offset by higher pre-tax income. The lower tax rate and lower pre-tax income were the main factors for the decrease in 1987.

The increase in other income in 1988 was mainly attributable to more cash available for short-term investments and higher interest rates. The decrease in 1987 primarily was due to lower interest rates and less cash available for short-term investments, as well as less interest on amounts recoverable from customers.

Income deductions increased in 1988, mainly as a result of the interest expense applicable to the \$20 million ten-year First Mortgage Bonds, 10.20% Series I, issued on December 1, 1987.

Liquidity and Capital Resources

The Company has access to outside capital markets and to internal sources of funds that together should provide sufficient resources to meet capital requirements. The Company does not anticipate any changes that materially would alter its current liquidity position.

Due to the seasonal nature of gas sales, a major portion of cash collections occurs between November and April. Because of timing differences in the receipt and disbursement of cash, and the level of construction requirements, the Company may borrow on a short-term basis. Short-term borrowings are either repaid with cash from operations or refinanced on a permanent basis with debt or equity, depending on money-market conditions and capital structure considerations.

The Company issued \$20 million ten-year First Mortgage Bonds, 10.20% Series I, on December 1, 1987. The proceeds were used to retire short-term debt and for capital expenditures.

Additional bonds are issuable by the Company, upon Illinois Commerce Commission approval, subject to limitations by certain restrictive provisions of the open-end mortgages and supplements thereto. These restrictions are not expected to have an impact on the Company's ability to issue additional debt, as needed. The Company does not expect to issue any new long-term debt in fiscal 1989. Short-term cash needs are met through borrowing arrangements with banks and/or the issuance of commercial paper. See Note (10) of Notes to Consolidated Financial Statements. The commercial paper of the Company enjoys the top rating from leading rating agencies.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Liquidity and Capital Resources (Continued)

The Company's coverage of fixed charges for fiscal 1988, 1987 and 1986 was 4.20, 4.45, and 4.91, respectively. In addition to the increase in long-term debt, the effect of weather on income was a significant factor in the changes in these ratios. The long-term debt of the Company is rated Aa3 by Moody's Investors Service and AA- by Standard and Poor's Corporation. There has been no change in either of these ratings since fiscal 1985.

Capital expenditures for additions, replacements, and improvements to the utility plant were \$14.1 million in 1988, \$14.5 million in 1987 and \$10.8 million in 1986. Capital expenditures for fiscal 1989 are estimated to be \$18.1 million.

In December 1987, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 96, "Accounting for Income Taxes". While earlier application was encouraged, the Company was not required to adopt the new accounting rules until fiscal 1990. In December 1988, the FASB issued SFAS No. 100, "Accounting for Income Taxes - Deferral of Effective Date of FASB 96". This statement deferred the effective date of SFAS No. 96 until fiscal 1991. The impact of SFAS No. 96 on the financial position of the Company is not expected to be significant. See Note (1)i of Notes to Consolidated Financial Statements.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

	<u>Page</u>
Report of Independent Public Accountants	14
Consolidated Statements of Income for the fiscal years ended September 30, 1988, 1987 and 1986	15
Consolidated Statements of Retained Earnings for fiscal years ended September 30, 1988, 1987 and 1986	15
Consolidated Balance Sheets as of September 30, 1988 and 1987	16
Consolidated Capitalization Statements as of September 30, 1988 and 1987	17
Consolidated Statements of Cash Flows for the fiscal years ended September 30, 1988, 1987 and 1986	18
Notes to Consolidated Financial Statements	19
Selected Quarterly Financial Data	30



REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To North Shore Gas Company:

We have audited the accompanying consolidated balance sheets and consolidated capitalization statements of North Shore Gas Company (an Illinois corporation, hereinafter referred to as the Company and a wholly-owned subsidiary of Peoples Energy Corporation) and subsidiary companies as of September 30, 1988 and 1987, and the related consolidated statements of income, retained earnings, and cash flows for each of the three years in the period ended September 30, 1988. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of North Shore Gas Company and subsidiary companies at September 30, 1988 and 1987, and the results of their operations and their cash flows for each of the three years in the period ended September 30, 1988, in conformity with generally accepted accounting principles.

As discussed in Note (4) of the Notes to Consolidated Financial Statements, the method of accounting for pensions was changed in fiscal year 1987.

Our audits were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The financial statement schedules listed in Item 14(a)2 are presented for purposes of complying with the Securities and Exchange Commission's rules and are not part of the basic financial statements. These financial statement schedules have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN & CO.

Chicago, Illinois  
November 2, 1988

North Shore Gas Company  
CONSOLIDATED STATEMENTS OF INCOME  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1988	1987	1986
OPERATING REVENUES:			
Gas sales	\$117,883	\$124,843	\$164,807
Transportation of customer-owned gas	4,990	2,523	7
Other	840	792	944
Total Operating Revenues	<u>123,713</u>	<u>128,158</u>	<u>165,758</u>
OPERATING EXPENSES:			
Gas costs	71,708	77,616	108,893
Operation	15,468	16,239	16,345
Maintenance	2,239	2,459	2,453
Depreciation	4,808	4,541	4,343
Taxes - Income	6,185	6,341	8,789
- State and local revenue	7,828	8,591	11,094
- Other	1,486	1,461	1,362
Total Operating Expenses	<u>109,722</u>	<u>117,248</u>	<u>153,279</u>
OPERATING INCOME	13,991	10,910	12,479
OTHER INCOME:			
Interest income	927	331	1,234
Allowance for funds used during construction	114	25	--
Miscellaneous	90	232	190
Total Other Income	<u>1,131</u>	<u>588</u>	<u>1,424</u>
GROSS INCOME	15,122	11,498	13,903
INCOME DEDUCTIONS:			
Interest on long-term debt	4,190	2,962	3,521
Other interest	848	1,032	1,080
Amortization of debt discount and expense	34	21	23
Miscellaneous	--	1	1
Total Income Deductions	<u>5,072</u>	<u>4,016</u>	<u>4,625</u>
NET INCOME	10,050	7,482	9,278
Preferred stock dividends	<u>270</u>	<u>299</u>	<u>378</u>
NET INCOME APPLICABLE TO COMMON STOCK	<u>\$ 9,780</u>	<u>\$ 7,183</u>	<u>\$ 8,900</u>

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1988	1987	1986
BALANCE AT BEGINNING OF YEAR	\$ 23,204	\$ 19,538	\$ 16,440
Add - Net Income	10,050	7,482	9,278
Deduct - Dividends on common stock	3,699	3,517	5,802
- Dividends on preferred stock	270	299	378
BALANCE AT END OF YEAR	<u>\$ 29,285</u>	<u>\$ 23,204</u>	<u>\$ 19,538</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company  
CONSOLIDATED BALANCE SHEETS  
(Thousands of Dollars)

	As of September 30,	
	1988	1987
<b>PROPERTIES AND OTHER ASSETS</b>		
<b>CAPITAL INVESTMENTS:</b>		
Property, plant and equipment, at original cost	\$163,985	\$151,020
Less - Accumulated depreciation	52,573	48,640
	<u>111,412</u>	<u>102,380</u>
Gas supply advances and investments	432	1,358
<b>TOTAL CAPITAL INVESTMENTS</b>	<u>111,844</u>	<u>103,738</u>
<b>CURRENT ASSETS:</b>		
Cash	415	596
Cash equivalents	2,500	1,000
Receivables -		
Customers, net of allowance for uncollectible accounts of \$646 and \$544, respectively	3,486	4,129
Other	29	39
Materials and supplies, at average cost	2,300	1,687
Gas in storage, at last-in, first-out cost	19,686	19,054
Gas costs recoverable through rate adjustments	135	118
Prepayments	489	598
<b>TOTAL CURRENT ASSETS</b>	<u>29,040</u>	<u>27,221</u>
<b>DEFERRED CHARGES</b>	<u>1,558</u>	<u>843</u>
<b>TOTAL PROPERTIES AND OTHER ASSETS</b>	<u>\$142,442</u>	<u>\$131,802</u>
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION (see accompanying statement)</b>	\$ 96,387	\$ 74,486
<b>CURRENT LIABILITIES:</b>		
Interim loans	--	11,500
Accounts payable	7,441	7,203
Dividends payable on common stock	1,341	--
Customer deposits	5,790	5,081
Sinking fund payments and maturities -		
Long-term debt	2,100	2,339
Accrued taxes	1,136	(214)
Gas sales revenue refundable	5,274	9,045
Accrued interest	1,067	214
<b>TOTAL CURRENT LIABILITIES</b>	<u>24,149</u>	<u>35,168</u>
<b>RESERVES AND DEFERRED CREDITS:</b>		
Deferred income taxes - primarily accelerated depreciation	16,318	15,758
Investment tax credits being amortized over the average lives of related property	4,967	5,099
Other	621	1,291
<b>TOTAL RESERVES AND DEFERRED CREDITS</b>	<u>21,906</u>	<u>22,148</u>
<b>TOTAL CAPITALIZATION AND LIABILITIES</b>	<u>\$142,442</u>	<u>\$131,802</u>

( ) Denotes red figure.

The accompanying notes are an integral part of these statements.

North Shore Gas Company  
CONSOLIDATED CAPITALIZATION STATEMENTS  
(Thousands of Dollars)

	<u>As of September 30,</u>	
	<u>1988</u>	<u>1987</u>
COMMON STOCKHOLDER'S EQUITY:		
Common stock, without par value		
Authorized 5,000,000 shares,		
Outstanding 3,625,887 shares	\$ 24,757	\$ 24,757
Retained earnings (see accompanying statement)	<u>29,285</u>	<u>23,204</u>
TOTAL COMMON STOCKHOLDER'S EQUITY	54,042	47,961
REDEEMABLE CUMULATIVE PREFERRED STOCK:		
Exclusive of sinking fund payments, due within one year		
Authorized 190,000 shares, par value \$100		
9% Series, 30,000 shares outstanding	<u>3,000</u>	<u>3,000</u>
TOTAL REDEEMABLE CUMULATIVE PREFERRED STOCK	3,000	3,000
LONG-TERM DEBT:		
Exclusive of sinking fund payments and maturities,		
due within one year		
First Mortgage Bonds -		
9-1/2% Series E, due February 1, 1995	6,101	6,375
8-3/8% Series F, due October 1, 1998	6,944	7,250
8-3/8% Series G, due February 15, 1992	1,800	2,400
12% Series H, due September 15, 1995	4,500	7,500
10.20% Series I, due October 27, 1997	<u>20,000</u>	<u>--</u>
TOTAL LONG-TERM DEBT	<u>39,345</u>	<u>23,525</u>
TOTAL CAPITALIZATION	<u>\$ 96,387</u>	<u>\$ 74,486</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company

CONSOLIDATED STATEMENTS OF CASH FLOWS  
(Thousands of Dollars)

	<u>For Fiscal Years Ended September 30,</u>		
	<u>1988</u>	<u>1987</u>	<u>1986</u>
<b>CASH FLOWS FROM OPERATING ACTIVITIES:</b>			
Net Income	\$ 10,050	\$ 7,482	\$ 9,278
Adjustments to reconcile net income to net cash:			
Depreciation	4,808	4,541	4,343
Deferred income taxes and investment tax credits - net	585	670	1,277
Change in deferred credits - refund to customers	(678)	678	--
Change in other deferred credits and reserves	(149)	3	(945)
Change in deferred charges	(715)	(61)	(50)
Amortization	136	207	284
Change in certain current assets and certain current liabilities:			
Receivables - net	652	1,392	10
Payables	238	(300)	(2,016)
Gas in storage	(632)	1,082	(1,180)
Rate adjustments refundable or recoverable	(3,788)	(896)	1,353
Accrued taxes	1,351	(1,306)	103
Customer deposits	709	262	(355)
Materials and supplies	(613)	(291)	(73)
Other	961	(221)	(321)
Total adjustments	<u>2,865</u>	<u>5,760</u>	<u>2,430</u>
<b>NET CASH PROVIDED BY OPERATING ACTIVITIES</b>	<u>12,915</u>	<u>13,242</u>	<u>11,708</u>
<b>CASH FLOWS FROM INVESTING ACTIVITIES:</b>			
Capital expenditures - construction	(14,144)	(14,539)	(10,810)
Other assets	305	919	130
Recovery of advance payments for gas supply	789	--	--
<b>NET CASH USED IN INVESTING ACTIVITIES</b>	<u>(13,050)</u>	<u>(13,620)</u>	<u>(10,680)</u>
<b>CASH FLOWS FROM FINANCING ACTIVITIES:</b>			
Retirement of long-term debt	(4,419)	(5,468)	(6,662)
Retirement of preferred stock	--	(1,000)	(1,000)
Interim loans - net	(11,500)	11,500	--
Issuance of long-term debt	20,000	--	--
Dividends paid on preferred stock	(270)	(310)	(388)
Dividends paid on common stock	(2,357)	(3,517)	(5,801)
<b>NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES</b>	<u>1,454</u>	<u>1,205</u>	<u>(13,851)</u>
<b>NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS</b>	1,319	827	(12,823)
<b>CASH AND CASH EQUIVALENTS AT BEGINNING OF YEAR</b>	<u>1,596</u>	<u>769</u>	<u>13,592</u>
<b>CASH AND CASH EQUIVALENTS AT END OF YEAR</b>	<u>\$ 2,915</u>	<u>\$ 1,596</u>	<u>\$ 769</u>

( ) Denotes red figure.

The accompanying notes are an integral part of these statements.

North Shore Gas Company

STATEMENT OF MANAGEMENT

These financial statements were prepared by management, which is responsible for their integrity and objectivity. The statements are in conformity with generally accepted accounting principles and, as such, reflect judgments made by management.

Based upon the Company's accounting and internal control systems, along with ongoing internal audit programs, management believes that the accounting records are reliable for the purpose of preparing financial statements, and assets are appropriately safeguarded against loss from unauthorized use.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) SIGNIFICANT ACCOUNTING POLICIES

a. Principles of Consolidation

All subsidiaries of the Company are included in the consolidated financial statements. All significant intercompany transactions have been eliminated in consolidation. Certain items previously reported for years prior to 1988 have been reclassified to conform with the current-year presentation.

b. Statement of Cash Flows

In accordance with Statement of Financial Accounting Standards (SFAS) No. 95, "Statement of Cash Flows", a statement of cash flows is presented in the financial statements for fiscal 1988, replacing the statement of changes in financial position previously included in the financial statements. Prior years' data have been restated to conform to the 1988 presentation in the Consolidated Statements of Cash Flows.

For purposes of the balance sheet and the statement of cash flows, the Company considers all short-term liquid investments with an original maturity of three months or less to be cash equivalents.

Interim loans, which are shown "net", represent short-term borrowings with a maturity of three months or less.

Income taxes paid were \$4.2 million, \$6.8 million and \$8.3 million in fiscal years 1988, 1987 and 1986, respectively. Interest paid (excluding capitalized interest) during the same periods was \$3.6 million, \$3.5 million and \$4.2 million, respectively.

c. Property, Plant and Equipment

Property, plant and equipment is stated at original cost and includes appropriate amounts of payroll taxes, employee-benefit costs, administrative costs, and an allowance for funds used during construction.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

d. Allowance for Funds Used During Construction

The assumed cost of all funds used to finance substantial and lengthy construction is capitalized as a cost element of Utility Plant, with an offsetting credit to Other Income. Under established regulatory practices, the Company is permitted to include in its rates a fair return on, and the recovery of, these capitalized costs by including them in rate base and in the provision for depreciation. The effect on fiscal years 1988 and 1987 net income of the allowance for funds used during construction is immaterial. There was no allowance for funds used during construction in fiscal year 1986.

e. Maintenance and Depreciation

The Company charges the cost of maintenance and repairs of property and minor renewals and improvements of property to maintenance expense. When depreciable property is retired, its original cost is charged to the accumulated provision for depreciation.

The provision for depreciation substantially reflects the systematic amortization of the original cost of depreciable property over the estimated useful lives on the straight-line method. Additionally, actual dismantling cost, net of salvage, is included in the provision for depreciation in the month incurred. The amounts provided are designed to cover not only losses due to wear and tear that are not restored by maintenance, but also losses due to obsolescence and inadequacy.

The provision for depreciation, expressed as an annual percentage of original cost of depreciable property, approximated 3.5%, 3.6% and 3.7% for fiscal years 1988, 1987 and 1986, respectively.

f. Revenue Recognition

Gas sales revenues for retail customers are recognized on the basis of monthly cycle billings and are recorded when customers are billed. Revenues for transportation customers are recorded based on month-end meter readings.

g. Recovery of Gas Costs

Under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or a current asset (with a contra entry to gas costs), and the fiscal year-end balance is amortized over the 12-month period beginning the following January 1.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

h. Gas in Storage

Storage injections are priced at the fiscal-year average of demand and commodity costs of natural gas purchased. Withdrawals from storage are priced on the last-in, first-out (LIFO) method. The estimated current replacement cost of gas in inventory, at September 30, 1988, and 1987, exceeded the LIFO cost by approximately \$22 million and \$25 million, respectively.

i. Taxes

For federal and Illinois income tax purposes, for periods prior to January 1, 1981, the Company adopted liberalized methods of computing depreciation on property additions after December 31, 1953, and the Asset Depreciation Range (ADR) system on property additions after December 31, 1970. For periods after December 31, 1980, the Company utilized the Accelerated Cost Recovery System (ACRS), and the Modified Accelerated Cost Recovery System (MACRS) on property additions after December 31, 1986.

Deferred income taxes for the difference between tax depreciation computed on these methods and straight-line depreciation are charged to income and credited to accumulated deferred income taxes. This account is charged when liberalized, ADR, ACRS, or MACRS tax depreciation becomes less than straight-line depreciation.

Investment tax credits have been deferred and are being amortized through credits to income over the book lives of related property. The Tax Reform Act of 1986, signed into law on October 22, 1986, repealed the investment tax credit for property placed in service after December 31, 1985, subject to certain transition rules.

At September 30, 1988, the cumulative net amount of timing differences for which deferred income taxes have been over provided is approximately \$.9 million.

The preceding deferred-tax and tax-credit accounting conforms with regulations of the Illinois Commerce Commission.

In December, 1987, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 96, "Accounting for Income Taxes". While earlier application was encouraged, the Company was not required to adopt the new accounting rules until fiscal 1990. In SFAS No. 96, the FASB retained the existing requirement to record deferred taxes for transactions that are reported in different years for financial reporting and tax purposes. These items, referred to as temporary differences in SFAS No. 96, also included differences between the book and tax bases of assets and liabilities. While comprehensive interperiod income tax allocation continues, the methodology and measurement of deferred income taxes



North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

i. Taxes (Continued)

have changed. The impact of SFAS No. 96 on the financial position of the Company is not expected to be significant. In December 1988, the FASB issued SFAS No. 100, "Accounting for Income Taxes - Deferral of Effective Date of FASB 96". This statement deferred the effective date of SFAS No. 96 until fiscal 1991.

j. Accounting for Pensions

Effective October 1, 1986, the Company adopted the provisions of SFAS No. 87, "Employers' Accounting for Pensions". Pension expense for fiscal 1987 was \$.8 million as compared to \$1.3 million for fiscal 1986 mainly due to the implementation of SFAS No. 87. Pension expense for fiscal 1988 was \$.6 million. See Note (4) of Notes to Consolidated Financial Statements.

k. Suppliers' Charges for Take-or-Pay Costs

The Illinois Commerce Commission has ordered that the utilities in the State defer on their books payments of charges to recover pipeline supplier take-or-pay costs. The charges are billed pursuant to a policy adopted in Federal Energy Regulatory Commission (FERC) Order No. 500. See Note (3) of Notes to Consolidated Financial Statements.

1. Illinois Residential Affordable Payment Program (IRAPP)

Under IRAPP, which was implemented in December 1985, the Company is prohibited from discontinuing gas service to any participating customer who pays the monthly obligation required by IRAPP (the monthly obligation). For the period December 1 through April 30, the monthly obligation is 8 per cent of the customer's income, and for the period May 1 through November 30 that obligation is the greater of 8 per cent of the customer's income or the full amount of the customer's current bill calculated under tariff provisions (the current bill). The difference between the current bill and the monthly obligation is referred to as "shortfall."

The Illinois Commerce Commission (Commission) has ruled that IRAPP participants are not at any time required to pay for the shortfall. Therefore, accumulated shortfall is excluded from gas sales and is reflected in deferred credits with a corresponding amount in deferred charges. Amounts representing shortfall are recognized as gas sales when recovered from sources other than IRAPP participants (such as governmental assistance programs). At September 30, 1988, the accumulated shortfall reflected in the deferred account was \$100,000. The Company cannot reasonably determine at this time the future impact of accumulated shortfall not recovered from sources other than IRAPP participants.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

1. Illinois Residential Affordable Payment Program (IRAPP) (Continued)

The State of Illinois has appropriated \$40 million to the Illinois Department of Commerce and Community Affairs to reimburse public utilities and other energy vendors for shortfall incurred under IRAPP or similar percentage of income payment plans. On August 3, 1988, the Commission initiated an investigation to determine the amounts of shortfall incurred under IRAPP through November 30, 1987, by the Company and other public utilities, for the purpose of determining the amount properly payable to each utility by the Illinois Department of Commerce and Community Affairs.

(2) COVENANTS REGARDING RETAINED EARNINGS

The Company's Indenture relating to the First Mortgage Bonds and the Stock Purchase Agreements relating to the Cumulative Preferred Stock contain provisions and covenants restricting the payment of cash dividends and the purchase or redemption of capital stock. At September 30, 1988, such restrictions amounted to \$4.4 million out of the Company's total retained earnings of \$29.3 million.

(3) RATES AND REGULATION

On December 22, 1987, the Illinois Commerce Commission (Commission) approved a filing made by the Company to make effective in January 1988, a one-time refund and prospective rate reduction. Pursuant to the terms of its filing, the Company refunded \$1.1 million via a credit to its customers' accounts on January 7, 1988, and has reduced rates effective January 1, 1988, to reflect a reduction in annual operating revenues (excluding additional charges for revenue taxes) of \$2.9 million. The rider to the Company's rate schedule that became effective in March 1987, which provided for recording of deferred credits relating to the reduction in the maximum federal income tax rate, has been terminated, except for provisions regarding the refund described above.

The Company's filing was the result of a dollar settlement agreement with several parties regarding the Company's rates, without agreement on the elements of cost of service, cost of common equity, or overall rate of return.

In April 1988, Natural Gas Pipeline Company of America (Natural) received permission from the Federal Energy Regulatory Commission (FERC) to recover from its utility customers, including the Company, by separate charges, certain of Natural's so-called "past" take-or-pay costs. These costs arise from the settlement of liabilities under agreements with producers that require Natural to pay for supplies it contracted for, whether or not it takes and subsequently sells them. Natural's recovery of these costs was approved pursuant to a policy adopted by the FERC in Order No. 500.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(3) RATES AND REGULATION (Continued)

By an Order dated April 27, 1988, the Commission initiated an investigation into the appropriate recovery by Illinois gas utilities of take-or-pay charges imposed by pipelines pursuant to Order No. 500, and ordered that the utilities defer payments of these costs on their books pending the resolution of this investigation.

By its Interim Order dated July 20, 1988, the Commission determined that it is precluded by law from prohibiting jurisdictional utilities from recovering unavoidable charges paid for pipeline take-or-pay costs approved by the FERC, pursuant to its Order No. 500 policy. The Commission ordered the scope of this preceeding limited to two questions: (1) should such charges for take-or-pay costs appropriately be recovered through the Uniform Gas Charge, and (2) from which classes of customers should the charges be recovered. The Company is of the opinion that the costs being investigated in this docket are gas costs fully recoverable through the Gas Charge.

Natural began billing these charges in May 1988. Such charges are anticipated to be in effect for a period ending between three to four years from their inception. The total amount of payments deferred by the Company in accordance with the Commission Order at September 30, 1988, was \$.7 million.

(4) PENSION PLANS AND POST-RETIREMENT BENEFITS

The Company participates in two defined benefit pension plans covering substantially all employees. These plans provide pension benefits that generally are based on an employee's length of service, compensation during the five years preceding retirement, and social security benefits. The Company makes annual contributions to the plans based upon actuarial determinations and in consideration of tax regulations and funding requirements under federal law.

The Company adopted Statement of Financial Accounting Standards (SFAS) No. 87, "Employers' Accounting for Pensions", effective October 1, 1986, which required a change in the actuarial cost method and certain other actuarial assumptions used in determining pension cost. These changes had the effect of reducing fiscal 1987 pension costs by \$.4 million compared to the previous method. Net pension cost under SFAS No. 87 for fiscal 1988 and 1987 includes the following components:

	<u>1988</u>	<u>1987</u>
	(Millions)	(Millions)
Service cost - benefits earned during year	\$ .7	\$ .7
Interest cost on projected benefit obligations	1.8	1.7
Actual return on plan assets	--	(4.8)
Net amortization and deferral	<u>(1.9)</u>	<u>3.2</u>
Net pension cost	<u>\$ .6</u>	<u>\$ .6</u>

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(4) PENSION PLANS AND POST-RETIREMENT BENEFITS (Continued)

The following assumptions were used in the calculation of pension cost:

	<u>1988</u>	<u>1987</u>
Weighted average discount rate	7.4%	6.9%
Long-term rate of return on assets	7.0	6.5
Rate of compensation increase	5.5	5.5

In accordance with the provisions of SFAS No. 87, pension expense, which was \$1.3 million for 1986, has not been restated.

At September 30, 1988 and 1987, the estimated funded status of the Company's pension plans was as follows:

	<u>1988</u>	<u>1987</u>
	(Millions)	
Actuarial present value of plan benefits:		
Vested	\$15.7	\$15.8
Nonvested	<u>1.6</u>	<u>1.9</u>
Accumulated benefit obligation	17.3	17.7
Effect of projected future compensation increases	<u>7.0</u>	<u>6.5</u>
Projected benefit obligation	24.3	24.2
Plan assets at market value	<u>27.7</u>	<u>29.1</u>
Plan assets in excess of projected benefit obligation	<u>\$ 3.4*</u>	<u>\$ 4.9*</u>
* Comprising:		
Effect of changes in assumptions and difference between actual and estimated experience	\$ 2.9	\$ 4.4
Unrecognized transition asset	<u>.5</u>	<u>.5</u>
	<u>\$ 3.4</u>	<u>\$ 4.9</u>

The projected benefit obligation was determined using weighted average discount rates of 7.6% and 7.4% as of year-end 1988 and 1987, respectively, and assumed future compensation increases of 5.5% for both years. Plan assets consist primarily of marketable equity and fixed income securities.

In addition to providing pension benefits, the Company provides certain health-care and life insurance benefits for retired employees. Substantially all employees may become eligible for such benefit coverage if they reach retirement age while working for the Company. The costs of providing these benefits are recognized as an expense during the period in which the costs are incurred. Such costs during fiscal years 1988, 1987, and 1986 were \$216,000, \$186,000 and \$154,000, respectively.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(5) TAX MATTERS

Provision for Income Taxes			
For fiscal years ended September 30,	1988	1987	1986
	(000's)		
Current:			
Federal	\$ 4,739	\$ 4,876	\$ 6,497
State	826	790	1,015
Total current income taxes	<u>5,565</u>	<u>5,666</u>	<u>7,512</u>
Deferred:			
Federal			
Accelerated depreciation	832	1,138	1,102
Rate refunds	221	(221)	--
Other	(408)	(181)	--
State	<u>127</u>	<u>102</u>	<u>162</u>
Total deferred income taxes	<u>772</u>	<u>838</u>	<u>1,264</u>
Investment tax credits - net:			
Federal	(239)	(248)	(21)
State	<u>52</u>	<u>80</u>	<u>34</u>
Total investment tax credits - net	<u>(187)</u>	<u>(168)</u>	<u>13</u>
Total provision for income taxes	6,150	6,336	8,789
Less - Included in other income or operation expense	<u>(35)</u>	<u>(5)</u>	<u>--</u>
Included in operating expenses as taxes - income	<u>\$ 6,185</u>	<u>\$ 6,341</u>	<u>\$ 8,789</u>

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(5) TAX MATTERS (Continued)

The following is a reconciliation between the computed federal income tax expense (tax rates of 34 per cent in 1988, 43 per cent in 1987, and 46 per cent in 1986, times pre-tax income) and the total provision for federal income tax expenses:

For fiscal years ended September 30,	1988		1987		1986	
	Amount (000's)	Per Cent of Pre-tax Income	Amount (000's)	Per Cent of Pre-tax Income	Amount (000's)	Per Cent of Pre-tax Income
Computed federal income tax expense	\$5,166	34.0	\$5,524	43.0	\$7,754	46.0
Amortization of investment tax credit	(239)	(1.6)	(248)	(1.9)	(249)	(1.5)
Out of period items at different tax rates	233	1.5	53	0.4	--	--
Book depreciation over depreciation used in tax provision	42	0.3	73	0.6	75	0.5
Other	<u>(57)</u>	<u>(0.4)</u>	<u>(38)</u>	<u>(0.3)</u>	<u>(2)</u>	<u>--</u>
Total provision for federal income taxes	<u>\$5,145</u>	<u>33.8</u>	<u>\$5,364</u>	<u>41.8</u>	<u>\$7,578</u>	<u>45.0</u>

( ) Denotes red figure.

Tax returns for 1980 through 1984 have been audited by the Internal Revenue Service and tax deficiencies of approximately \$1.4 million have been proposed. Issues are being contested, and the potential impact on net income is not believed to be material, since the issues consist of income tax provision timing differences.

Tax returns for 1985 and 1986 are currently under audit by the Internal Revenue Service.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(6) DEFERRED CHARGES

	As of September 30,	
	1988	1987
	(000's)	
Debt expense being amortized over the lives of outstanding issues	\$ 292	\$ 152
Energy Conservation Plan expenses	119	95
Interest on gas sales revenue refundable	184	381
IRAPP shortfall amounts	96	54
Payment of charges for pipeline suppliers' take-or-pay costs	720	--
Unamortized discount - notes payable	--	62
Other	147	99
	<u>\$1,558</u>	<u>\$ 843</u>

(7) REDEEMABLE CUMULATIVE PREFERRED STOCK

	<u>9.0% Series</u>
Year of issue	1980
Shares outstanding	30,000
Involuntary liquidation preference (000's)	\$ 3,000
Annual dividends per share	\$ 9.00
Redemption options:	
Currently effective redemption price per share	(a)
Redemption price per share decreases annually to issue price by (year)	(a)
Redemption through certain refunding operations not permitted prior to (year)	1990

(a) Not currently redeemable at the option of the Company.

(8) COMMON STOCK

No common stock was issued during the fiscal years 1986 through 1988.

(9) SINKING FUND REQUIREMENTS

There are no sinking fund requirements for the preferred stock outstanding at September 30, 1988. The preferred stock outstanding at September 30, 1988 is required to be redeemed in its entirety, \$3.0 million, on its redemption date of October 1, 1990.

Sinking fund requirements and maturities of long-term debt outstanding at September 30, 1988, for fiscal years 1989 through 1993 are \$2.1 million for 1989, \$2.3 million for 1990, \$2.5 million for 1991, \$2.6 million for 1992 and \$0.5 million for 1993.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(10) SHORT-TERM BORROWING AND COMPENSATING BALANCES

Short-term cash needs of the Company are met through bank loans and/or the issuance of commercial paper. The outstanding total amount of these borrowings cannot at any time exceed total bank credit then in effect.

During fiscal 1988, Peoples Gas maintained \$63 million in bank credit through an irrevocable revolving credit agreement. This amount has been secured for fiscal 1989 and 1990. The Company may borrow up to \$15 million.

Payment for the revolving credit agreement with the banks is through compensating balances and/or fees. There are no legal restrictions on withdrawal of compensating balances.

For additional information on short-term borrowings, see Schedule IX.

(11) CAPITAL COMMITMENTS

Total contract and purchase order commitments of the Company at September 30, 1988, amounted to approximately \$3.3 million.

(12) ASSETS SUBJECT TO LIEN

The Indenture of Mortgage, dated April 1, 1955, as supplemented, securing the First Mortgage Bonds issued by the Company, constitutes a direct, first-mortgage lien on substantially all property owned by the Company.

(13) EXPLORATION SUBSIDIARY

North Shore Exploration Company, a wholly-owned subsidiary of the Company, was formed in 1973 to engage, directly or indirectly, in lease-acquisition, exploration and development programs. The subsidiary has made investments totaling \$4.1 million and through September 30, 1988, has amortized \$3.7 million. The Company is allowed by the Illinois Commerce Commission to include such investments in its rate base and treat any profits or losses as utility transactions.

Currently, the exploration company owns small interests in the net profits of leased hydrocarbon-producing offshore blocks through six separate agreements. The exploration company receives monthly distributions of its portion of net profits. In fiscal 1988, these cash distributions totaled \$.5 million. Amortization of the investment for this same period totaled \$.1 million. No other business activity occurred during the fiscal year. The last investment in this venture was made in fiscal 1975, and no additional investments are anticipated.



North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(14) LEGAL PROCEEDINGS

There are no material legal proceedings pending to which the Company is a party.

(15) SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	<u>Operating Revenues</u>	<u>Operating Income</u> (000's)	<u>Net Income Applicable to Common Stock</u>
First Quarter			
1988	\$ 32,767	\$ 4,176	\$ 2,993
1987	37,092	3,575	2,411
Second Quarter			
1988	57,941	8,383	7,161
1987	54,782	6,379	5,358
Third Quarter			
1988	23,163	2,165	1,272
1987	25,326	1,662	888
Fourth Quarter			
1988	9,842	(733)	(1,646)
1987	10,958	(706)	(1,474)
Fiscal Year			
1988	123,713	13,991	9,780
1987	128,158	10,910	7,183

( ) Denotes red figure.

(16) EVENT SUBSEQUENT TO DATE OF FINANCIAL STATEMENTS

Reference is made to Note (3), "Rates and Regulations", of Notes to Consolidated Financial Statements.

On November 22, 1988, the Illinois Commerce Commission (Commission), issued an Order allowing state gas utilities, including the Company, to recover direct charges billed by pipeline suppliers for take-or-pay costs through the Uniform Gas Charge. The Commission further ruled that these charges may be recovered from all classes of customers.

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY

IDENTIFICATION OF DIRECTORS

<u>Name, Principal Occupation and Other Directorships</u>	<u>Age at 12-07-88</u>	<u>Company Directorship Since</u>
J. Bruce Hasch Executive Vice President of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	50	1986
James Hinchliff Vice President and General Counsel of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas.	48	1985
Donald G. Holm Vice President, Secretary and Treasurer of the Company and Peoples Gas; Vice President, Controller, Secretary and Treasurer of Peoples Energy; Director of Peoples Gas.	61	1982
Michael S. Reeves Executive Vice President of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas.	53	1987
Richard E. Terry President and Chief Operating Officer of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	51	1982
Eugene A. Tracy Chairman of the Board and Chief Executive Officer of the Company, Peoples Energy and Peoples Gas; Director of LaSalle National Bank.	60	1978

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY (Continued)

IDENTIFICATION OF EXECUTIVE OFFICERS

	<u>Position at December 7, 1988</u>	<u>Age at 12-07-88</u>	<u>Position Held Since</u>
Patrick J. Doyle	Vice President	51	1985
J. Bruce Hasch	Executive Vice President	50	1985
James Hinchliff	Vice President and General Counsel	48	1984
Donald G. Holm	Vice President, Secretary and Treasurer	61	1981
John A. Lawrisuk	Vice President	60	1981
John F. Mooney	Vice President	54	1987
Michael S. Reeves	Executive Vice President	53	1987
Richard E. Terry	President and Chief Operating Officer	51	1987
Eugene A. Tracy	Chairman of the Board and Chief Executive Officer	60	1981

Directors and executive officers of the Company were elected to serve for a term of one year or until their successors are duly elected and qualified.

There are no family relationships between directors and executive officers of the Company.

All of the directors and executive officers of the Company have been continuously employed by the Company and/or its affiliates in various capacities for at least 10 years.

## ITEM 11. EXECUTIVE COMPENSATION

The executive officers of the Company serve both the Company and its affiliate Peoples Gas. Remuneration is paid by Peoples Gas with appropriate amounts billed to the Company for the time such officers serve North Shore. The Company was billed \$309,293 for the services of these officers during fiscal 1988, including approximately \$67,000 for the services of Mr. Tracy. No other executive officer's cash remuneration for service to North Shore exceeded \$60,000. Information regarding executive compensation paid by Peoples Gas and its affiliates to Peoples Gas officers is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1988.

### Compensation of Directors

All directors of the Company were officers of the Company who received no compensation for serving as directors.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

### SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

As of November 30, 1988, voting securities of the Company were beneficially owned as follows:

<u>Name and Address</u>	<u>Number of Shares Owned</u>	<u>Per Cent of Class</u>
<u>Common Stock without par value</u>		
Peoples Energy Corporation 122 South Michigan Avenue Chicago, Illinois 60603	<u>3,625,887</u>	<u>100%</u>
<u>Redeemable Cumulative Preferred Stock, \$100 Par Value</u>		
GMAC Commercial Corporation General Motors Building 3044 West Grand Boulevard Detroit, Michigan 48202	<u>30,000</u>	<u>100%</u>

### SECURITY OWNERSHIP OF MANAGEMENT

No equity securities of the Company are beneficially owned directly or indirectly by any director or officer of the Company.

Information regarding Common Stock, without par value, of Peoples Energy beneficially owned directly or indirectly by directors and executive officers of the Company is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1988.

### CHANGES IN CONTROL

None.

## ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

None.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

	<u>Page</u>
(a) 1. Financial Statements:	
See Part II, Item 8.	13
2. Financial Statement Schedules:	
<u>Schedule</u> <u>Number</u>	
V           Property, Plant and Equipment at Original Cost	35
VI          Accumulated Provision for Depreciation of	
Property, Plant and Equipment	37
VIII       Valuation and Qualifying Accounts	38
IX          Short-Term Borrowings	40
X           Supplementary Income Statement Information	41
3. Exhibits:	
See Exhibit Index on page 43.	
(b) Reports on Form 8-K filed during the final quarter of fiscal year 1988:	
None.	

North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 1 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<u>Fiscal Year Ended September 30, 1988</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,850	\$ 133	\$ 17	\$ --	\$ 3,966
Storage plant	7,484	--	--	--	7,484
Distribution plant	129,910	8,211	685	--	137,436
General plant	7,980	889	477	--	8,392
Construction work in progress	1,071	4,911	--	--	5,982
Gas stored underground - noncurrent	<u>725</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>725</u>
Total public utility facilities	151,020	14,144	1,179	--	163,985
Nonutility property	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>--</u>
Total property, plant and equipment, at original cost	<u>\$151,020</u>	<u>\$ 14,144</u>	<u>\$ 1,179 (a)</u>	<u>\$ --</u>	<u>\$163,985</u>
<u>Fiscal Year Ended September 30, 1987</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,843	\$ 18	\$ 1	\$ (10)	\$ 3,850
Storage plant	7,271	213	--	--	7,484
Distribution plant	116,828	13,547	666	201	129,910
General plant	7,936	1,057	812 (b)	(201)	7,980
Construction work in progress	1,392	(321)	--	--	1,071
Gas stored underground - noncurrent	<u>701</u>	<u>24</u>	<u>--</u>	<u>--</u>	<u>725</u>
Total public utility facilities	137,971	14,538	1,479	(10) (c)	151,020
Nonutility property	<u>630</u>	<u>--</u>	<u>640</u>	<u>10</u>	<u>--</u>
Total property, plant and equipment, at original cost	<u>\$138,601</u>	<u>\$ 14,538</u>	<u>\$ 2,119 (a)</u>	<u>\$ --</u>	<u>\$151,020</u>

North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 2 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<u>Fiscal Year Ended September 30, 1986</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,798	\$ 45	\$ --	\$ --	\$ 3,843
Storage plant	6,793	478	--	--	7,271
Distribution plant	108,633	8,922	727	--	116,828
General plant	7,087	1,098	249	--	7,936
Construction work in progress	1,178	214	--	--	1,392
Gas stored underground - noncurrent	<u>648</u>	<u>53</u>	<u>--</u>	<u>--</u>	<u>701</u>
Total public utility facilities	128,137	10,810	976	--	137,971
Nonutility property	<u>630</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>630</u>
Total property, plant and equipment, at original cost	<u>\$128,767</u>	<u>\$ 10,810</u>	<u>\$ 976 (a)</u>	<u>\$ --</u>	<u>\$138,601</u>

( ) Denotes red figure.

Notes: (a) Represents:

	<u>1988</u>	<u>1987</u>	<u>1986</u>
Retirements charged to accumulated provision for depreciation Schedule (VI)	\$1,179	\$1,479	\$976
Cost of land retired at Peterson Road	<u>--</u>	<u>640</u>	<u>--</u>
	<u>\$1,179</u>	<u>\$2,119</u>	<u>\$976</u>

(b) Includes \$261,000 applicable to a change in minimum capitalization from \$250 to \$500.

(c) Represents the transfer of Peterson Road land to Nonutility property.

## North Shore Gas Company and Subsidiary Companies

## ACCUMULATED PROVISION FOR DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

(000's)

Column A	Column B	Column C		Column D			Column E	Column F
Description	Balance at beginning of period	Additions charged to costs and expenses (a)		Deduct retirements			Other changes	Balance at end of period
		Depreciation expense	Clearing accounts	Retirement of property at cost	Cost of dismantling	Stores and miscellaneous (salvage)		
Fiscal Year Ended September 30, 1988								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 2,261	\$ 125	\$ --	\$ 18	\$ --	\$ --	\$ --	\$ 2,368
Storage plant	2,068	253	--	--	--	--	--	2,311
Distribution plant	41,636	4,253	--	684	183	(1)	--	45,023
General plant	2,685	177	402	477	3	(87)	--	2,871
Total accumulation provision for depreciation	\$48,640	\$4,808	\$402	\$1,179	\$186	\$ (88)	\$ --	\$52,573
Fiscal Year Ended September 30, 1987								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 2,132	\$ 130	\$ --	\$ 1	\$ --	\$ --	\$ --	\$ 2,261
Storage plant	1,805	253	--	--	--	--	--	2,058
Distribution plant	38,487	3,934	--	666	198	(2)	77	41,636
General plant	2,875	224	389	812 (b)	--	(73)	(64)	2,685
Total accumulation provision for depreciation	\$45,299	\$4,541	\$389	\$1,479	\$198	\$ (75)	\$ 13 (c)	\$48,640
Fiscal Year Ended September 30, 1986								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 2,002	\$ 130	\$ --	\$ --	\$ --	\$ --	\$ --	\$ 2,132
Storage plant	1,562	243	--	--	--	--	--	1,805
Distribution plant	35,733	3,744	--	727	271	(8)	--	38,487
General plant	2,506	226	376	249	13	(29)	--	2,875
Total accumulation provision for depreciation	\$41,803	\$4,343	\$376	\$976	\$284	\$ (37)	\$ --	\$45,299

( ) Denotes red figure.

Notes: (a) See Note (1)e of Notes to Consolidated Financial Statements with respect to the basis for the provision for depreciation.

(b) Includes \$261,000 applicable to a change in minimum capitalization from \$250 to \$500.

(c) Represents the following:

	1987
Accumulated provision for depreciation applicable to property acquired	\$ 2
Proceeds from sale of property	11
	411



VALUATION AND QUALIFYING ACCOUNTS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance</u> <u>at beginning</u> <u>of period</u>	<u>Additions</u> <u>Charged</u> <u>to costs</u> <u>and</u> <u>expenses</u>	<u>Deductions</u> <u>Charges for the</u> <u>purpose for which the</u> <u>reserves or deferred</u> <u>credits were created</u>	<u>Balance</u> <u>at end of</u> <u>period</u>

For Fiscal Year Ended September 30, 1988

## RESERVES (deducted from assets in balance sheet):

Uncollectible items

\$ 544

\$ 842

\$ 740

\$ 646

## RESERVES (not deducted from assets in balance sheet) AND

## DEFERRED CREDITS:

Injuries and damages

\$ --

\$ 162

\$ 162

\$ --

Pensions

24

2

4

22

Possible refund to customers

678

433

1,111

--

IRAPP shortfall amounts (a)

54

146

104

96

Other

535

685

718

502

Total

\$1,291

\$1,428

\$2,099

\$ 620

For Fiscal Year Ended September 30, 1987

## RESERVES (deducted from assets in balance sheet):

Uncollectible items

\$ 634

\$ 903

\$ 993

\$ 544

## RESERVES (not deducted from assets in balance sheet) AND

## DEFERRED CREDITS:

Injuries and damages

\$ --

\$ 72

\$ 72

\$ --

Pensions

26

2

4

24

Possible refund to customers

--

678

--

678

IRAPP shortfall amounts (a)

(5)

157

98

54

Other

607

1,324

1,396

535

Total

\$ 628

\$2,233

\$1,570

\$1,291

North Shore Gas Company and Subsidiary Companies

Schedule VIII

Page 2 of 2

VALUATION AND QUALIFYING ACCOUNTS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance</u> <u>at beginning</u> <u>of period</u>	<u>Additions</u> <u>Charges</u> <u>to costs</u> <u>and</u> <u>expenses</u>	<u>Deductions</u> <u>Charges for the</u> <u>purpose for which the</u> <u>reserves or deferred</u> <u>credits were created</u>	<u>Balance</u> <u>at end of</u> <u>period</u>
<u>For Fiscal Year Ended September 30, 1986</u>				
RESERVES (deducted from assets in balance sheet):				
Uncollectible items	\$ 714	\$ 991	\$ 1,071	\$ 634
RESERVES (not deducted from assets in balance sheet) AND				
DEFERRED CREDITS:				
Injuries and damages	\$ --	\$ 227	\$ 227	\$ --
Pensions	29	3	6	26
IRAPP shortfall amounts (a)	--	--	5	(5)
Other	<u>739</u>	<u>544</u>	<u>676</u>	<u>607</u>
Total	<u>\$ 768</u>	<u>\$ 774</u>	<u>\$ 914</u>	<u>\$ 628</u>

( ) Denotes red figure.

(a) See Note (1) of Notes to Consolidated Financial Statements.

North Shore Gas Company and Subsidiary CompaniesSHORT-TERM BORROWINGS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E (a)</u>	<u>Column F (b)</u>
<u>Category of Aggregate Short-Term Borrowings</u>	<u>Balance at End of Period</u>	<u>Weighted Average Interest Rate</u>	<u>Maximum Amount Outstanding During the Period</u>	<u>Average Amount Outstanding During the Period</u>	<u>Weighted Average Interest Rate During the Period</u>
<u>Fiscal Year Ended September 30, 1988</u>					
Commercial Paper	\$ --	--	\$13,500	\$2,000	7.06%
<u>Fiscal Year Ended September 30, 1987</u>					
Commercial Paper	\$11,500	7.28%	\$11,500	\$1,726	6.87%

(a) Computed by multiplying the amounts outstanding by the days outstanding and dividing the results by the number of days used in accordance with the loan agreement.

(b) Computed by dividing the applicable interest expense by the average amount outstanding during the period.

There were no short-term borrowings in fiscal 1986.

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NORTH SHORE GAS COMPANY

Date: December 23, 1988

By: E. A. TRACY  
E. A. Tracy  
Chairman of the Board and Chief  
Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on December 23, 1988.

<u>E. A. TRACY</u> E. A. Tracy	Chairman of the Board and Chief Executive Officer and Director (Principal Executive Officer)
<u>D. G. HOLM</u> D. G. Holm	Vice President, Secretary and Treasurer and Director (Principal Financial and Accounting Officer)
<u>J. B. HASCH</u> J. B. Hasch	Director
<u>JAMES HINCHLIFF</u> James Hinchliff	Director
<u>MICHAEL S. REEVES</u> Michael S. Reeves	Director
<u>RICHARD E. TERRY</u> Richard E. Terry	Director

North Shore Gas Company and Subsidiary CompaniesSUPPLEMENTARY INCOME STATEMENT INFORMATION

Maintenance, depreciation, royalties, advertising costs and research and development costs, other than those specifically disclosed in the Consolidated Statements of Income, are not significant.

Significant taxes, other than taxes on income, including those charged to clearing and other accounts, are summarized as follows:

	<u>Fiscal Years Ended September 30,</u>		
	<u>1988</u>	<u>1987</u>	<u>1986</u>
		(000's)	
Real estate, invested capital, personal property, state capital stock and state franchise	\$ 1,008	\$ 945	\$ 927
Illinois public utility	5,098	5,322	6,800
Municipal public utility	2,633	3,176	4,173
Social security	649	712	614
Other	<u>314</u>	<u>308</u>	<u>311</u>
Total	<u>\$ 9,702</u>	<u>\$10,463</u>	<u>\$12,825</u>

North Shore Gas Company and Subsidiary Companies

EXHIBIT INDEX

- (a) The exhibits listed below are filed herewith and made a part thereof:

<u>Exhibit Number</u>	<u>Description of Document</u>	<u>Page Number</u>
3-a	Amendment to the By-Laws of the Registrant, dated March 31, 1988.	44
3-b	By-Laws, as last amended, dated March 31, 1988.	45

- (b) Exhibits listed below have been filed heretofore with the Securities and Exchange Commission pursuant to the Securities Act of 1933, as amended, and/or the Securities Exchange Act of 1934, as amended, and are incorporated herein by reference. The file number and exhibit number of each such exhibit are stated in the description of such exhibits.

<u>Exhibit Number</u>	<u>Description of Document</u>
3-c	Articles of Incorporation of the Registrant as amended on April 13, 1987 (Registrant Form 10-K for fiscal year ended September 30, 1987, Exhibit 3-b).
4-a	Indenture, dated as of April 1, 1955, from the Company to Continental Illinois National Bank and Trust Company of Chicago as Trustee; Third Supplemental Indenture, dated as of December 20, 1963 (North Shore-File No. 2-35965, Exhibit 4-1); Fifth Supplemental Indenture, dated as of February 1, 1970 (File No. 2-35965, Exhibit 4-2); Sixth Supplemental Indenture, dated as of October 1, 1973 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-3); Seventh Supplemental Indenture, dated as of February 15, 1977 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-4); Eighth Supplemental Indenture, dated as of September 15, 1980 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-5); and Ninth Supplement Indenture, dated as of December 1, 1987 (Form 10-K for the fiscal year ended September 30, 1987, Exhibit 4).

---

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM 10-K**

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 1987      Commission File Number 2-35965

**NORTH SHORE GAS COMPANY**

(Exact name of registrant as specified in its charter)

**Illinois**

(State or other jurisdiction of  
incorporation or organization)

**36-1558720**

(IRS Employer  
Identification No.)

**122 South Michigan Avenue, Chicago, Illinois**

(Address of principal executive offices)

**60603**

(Zip Code)

**Registrant's telephone number, including area code:**

**(312) 431-4000**

**Securities registered pursuant to Section 12(b) of the Act:    None**

**Securities registered pursuant to Section 12(g) of the Act:    None**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.    Yes   X      No     

State the aggregate market value of the voting stock held by non-affiliates of the registrant:

Redeemable Cumulative Preferred Stock, \$3,000,000 at November 30, 1987, based on the price at which the stock was sold.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, without par value, 3,625,887 shares outstanding at November 30, 1987.

Documents Incorporated by Reference

None

---

## CONTENTS

<u>Item No.</u>		<u>Page No.</u>
	<u>Part I</u>	
1.	Business	3
2.	Properties	9
3.	Legal Proceedings	9
4.	Submission of Matters to a Vote of Security Holders	9
	<u>Part II</u>	
5.	Market for the Company's Common Stock and Related Stockholder Matters	10
6.	Selected Financial Data	10
7.	Management's Discussion and Analysis of Results of Operations and Financial Condition	11
8.	Financial Statements and Supplementary Data	13
9.	Changes in and Disagreements with Accountants on Accounting and Financial Disclosure	13
	<u>Part III</u>	
10.	Directors and Executive Officers of the Company	29
11.	Executive Compensation	31
12.	Security Ownership of Certain Beneficial Owners and Management	31
13.	Certain Relationships and Related Transactions	32
	<u>Part IV</u>	
14.	Exhibits, Financial Statement Schedules and Reports on Form 8-K	33
	Signatures	41
	Exhibit Index	42



North Shore Gas Company

ANNUAL REPORT ON FORM 10-K

FISCAL YEAR ENDED SEPTEMBER 30, 1987

PART I

ITEM 1. BUSINESS

GENERAL

North Shore Gas Company (Company) is an operating public utility engaged primarily in the purchase, storage, distribution, sale and transportation of natural gas at retail to more than 106,000 residential, commercial and industrial customers within its service area of approximately 275 square miles, located in northeastern Illinois. It serves 56 communities and adjacent areas, including those situated along Lake Michigan from Winnetka, Illinois to the Illinois-Wisconsin state line. This area, with an estimated population of 354,000, contains residential concentrations and a diversity of industrial and commercial establishments, as well as some farm lands. The Company had 237 employees at September 30, 1987.

The Company holds certificates of public convenience and necessity issued by the Illinois Commerce Commission (Commission) for the conduct by the Company of its operations in the territory which it serves. It holds a license agreement from Lake County, Illinois, and, with minor exceptions, franchises from all of the incorporated cities and villages in its service territory. The franchises are of various terms and expiration dates, and are generally subject to various other conditions, restrictions or limitations not deemed materially burdensome.

At September 30, 1987, the common stock of the Company and of its affiliate, The Peoples Gas Light and Coke Company (Peoples Gas), was wholly-owned by Peoples Energy Corporation (Peoples Energy).

COMPETITION

Competition in varying degrees exists between natural gas and other fuels or forms of energy available to consumers in the Company's service area. Natural gas prices declined during the last year enabling gas to maintain a lower price than competing energies, except for certain fuel oils usable on a large volume basis by a small number of customers with dual-fuel capability. Overall, natural gas prices in the Company's service area compared very favorably on a national basis. The possibility of new or improved sources or uses of energy, limitations on future gas supply, changes in relative prices of competing fuels and energy, changes in environmental controls, increased use of transportation and other factors could, in the future, affect the Company's business. See "Federal Legislation and Regulation".

## ITEM 1. BUSINESS (Continued)

### SALES AND RATES

The Company sells natural gas having an average heating value of approximately 1,000 British thermal units (Btu's) per cubic foot.\* Sales are made and service rendered by the Company pursuant to a rate schedule on file with the Commission containing various service classifications largely reflecting customers' different uses and size of consumption. Monthly adjustments to the Gas Charge under the Company's rate schedule provide for the pass-through of increases or decreases in natural gas supplier rates, purchased storage service costs, transportation charges, liquefied petroleum gas costs and purchases of synthetic natural gas (SNG). In addition, under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or a current asset (with a contra entry to gas costs), and the fiscal year-end balance is amortized over the 12-month period beginning the following January 1.

The basic marketing plan of the Company is to seek expansion in all of its market areas.

### STATE LEGISLATION AND REGULATION

The Company is subject to the jurisdiction of and regulation by the Commission, which has general supervisory and regulatory powers over practically all phases of the public utility business in Illinois, including rates and charges, issuance of securities, services and facilities, systems of accounts, investments, safety standards, transactions with affiliated interests, as defined in the Illinois Public Utilities Act, and other matters.

Under the Illinois Residential Affordable Payment Program (IRAPP), the Company is prohibited from discontinuing gas service to any participating customer who pays the monthly obligation required by IRAPP. See Note (1)i of Notes to Consolidated Financial Statements.

The Company filed with the Commission a new rider to its rate schedule which became effective March 1, 1987, to provide for recording deferred credits relating to the reduction in the maximum federal income tax rate under the Tax Reform Act of 1986. See Note (3) and Note (17) of Notes to Consolidated Financial Statements.

The Commission has adopted the federal safety standards established under the Natural Gas Pipeline Safety Act of 1968 and is enforcing such standards with respect to the Company. The Company has a continuing program of inspection designed to keep all of its facilities in compliance with pipeline safety and pollution control requirements. The Company has made a complete inspection of all of its operational facilities and to the best of its knowledge is in substantial compliance with all pipeline safety and pollution control requirements.

---

\* All volumes of natural gas set forth in this report are stated on a 1,000 Btu (per cubic foot) billing basis.

ITEM 1. BUSINESS (Continued)

FEDERAL LEGISLATION AND REGULATION

By Order entered on December 6, 1968 (Holding Company Act Release No. 16233), the Securities and Exchange Commission (SEC), pursuant to Section 3(a)(1) of the Public Utility Holding Company Act of 1935 (Act) exempted Peoples Energy and its subsidiary companies as such (including the Company) from the provisions of the Act other than Section 9(a)(2) thereof.

The Natural Gas Policy Act (NGPA), a major part of the National Energy Act enacted in 1978, instituted important changes in the laws affecting the natural gas industry. The NGPA (1) established ceiling prices at the wellhead for both interstate and previously unregulated intrastate gas, (2) deregulated the wellhead price of certain "high-cost" gas as of November 1, 1979, (3) deregulated the wellhead price of a major portion of the nation's gas supplies as of January 1, 1985, and (4) deregulated the wellhead prices of gas in other categories in 1987. No material financial impact has resulted for the Company from NGPA deregulation provisions.

In late 1985, and early 1986, the FERC issued Order Nos. 436 and 436-A through E which, among other things, offered pipelines an option to transport gas on an "open-access" nondiscriminatory basis for all shippers under expedited regulatory procedures. Pipelines that elected this option were required, as a condition thereto, to allow firm sales customers to reduce their gas purchase demand volumes under firm sales contracts or convert such purchase demand volumes to firm transportation service by up to 100 per cent over a five-year period following the pipeline's election.

In June 1987, the D.C. Circuit Court of Appeals determined that the 436 series of orders should be vacated and remanded to the FERC for further consideration. Early in August, a number of parties requested rehearing of the Court's decision. Meanwhile, in response to the Court's decision, the FERC in August issued Order No. 500 which readopts on an interim basis the regulations promulgated by Order No. 436 with certain modifications intended to address the Court's concerns. Order No. 500 also establishes procedures for public comment and issuance of a final rule on remanded issues. The principal modifications to the Order No. 436 regulations adopted in Order No. 500 are: (1) a requirement that producers grant take-or-pay credits to pipelines transporting their gas; (2) a policy as to the acceptable mechanism for the passthrough to pipeline customers of take-or-pay buyout and buydown costs; (3) principles upon which pipelines may charge customers for the cost of holding gas supplies to serve them; and (4) elimination of the pipeline customer's option to reduce contract demand. Order No. 500 has been appealed to the Courts.

A number of the customers of the Company are substituting customer-owned gas for gas purchases from the Company, utilizing the availability of pipeline transportation as well as the Company's own transportation services. Under existing rates, the Company will experience no loss of distribution margin due to customer shifts from gas service to transportation service. The Company has utilized the increased availability of transportation to make purchases in the competitive spot market, thereby reducing the average cost of gas that must be recovered from customers.

ITEM 1. BUSINESS (Continued)

FEDERAL LEGISLATION AND REGULATION (Continued)

Despite the access to spot market supplies afforded by open-access transportation, the Company is concerned because it is not known how the changing use of pipeline services under the new open-access rules will affect the security and reliability of long-term supplies from pipelines for distributors.

A pipeline may seek to provide transportation service directly to end-users. Such direct service by a pipeline to an end-user would bypass the local distributor's service and reduce its earnings. However, no such service has yet been proposed under this new rule for any customers of the Company.

In December 1986, the FERC voted to deny rehearing of Order No. 451, which raised the ceiling prices permitted to be paid for all categories of "old" gas, still regulated under the NGPA, to that of the highest-priced old gas category. The order also established a "good faith negotiation" procedure by which producers of such gas may seek increased prices up to the new ceiling. A portion of contracted gas reserves of the pipeline supplier for the Company is subject to this rule. At this time, the Company cannot determine the ultimate impact on customers gas bills of Order No. 451, which is under appeal to the Federal courts.

On August 5, 1987, Natural Gas Pipeline of America (Natural), the sole pipeline supplier of the Company, filed an application seeking FERC authority to abandon 20 per cent of its firm contract sales obligation to the Company and all of Natural's utility customers. Natural proposes to replace the abandoned portion of its sales obligation with an equal amount of firm transportation capacity. Approval of the plan by the FERC would effectively make Natural's utility customers responsible for arranging for commitments from other suppliers of up to one-fifth of the supplies they can now elect to buy on a firm daily basis from Natural. Based on information available to it at this time, the Company is opposed to Natural's application. Because the proceedings related to Natural's filing are in their initial phase, the potential effect on the Company cannot be determined at this time.

On September 15, 1987, Natural filed with the FERC revised tariff sheets instituting an inventory holding charge for the alleged purpose of recovering the costs of maintaining a gas supply inventory to meet the peak day, monthly and annual service levels of its DMQ-1 and G-1 customers. The Company is opposed to Natural's filing because the proposed charge is excessive and does not comply with the requirements of Order No. 500. The FERC suspended the filing for the maximum period permitted by law, until April 1, 1988, and has ordered an expedited procedural schedule which will enable it to make a final decision, after hearing, by the April 1 date.

## ITEM 1. BUSINESS (Continued)

### GAS SUPPLY ADVANCES AND INVESTMENTS

During the natural gas shortage of the 1970's, the Company undertook several programs to augment its gas supply. From 1971 through 1981, the Company, with Commission approval, made advance payments through a pipeline supplier and equity investments in gas and oil exploration and development ventures. At September 30, 1987, \$1.3 million in advances and equity investments remain outstanding. The Company is allowed by the Commission to include such advances and investments in the rate base and treat any profits or losses as utility transactions. See Note (13) of Notes to Consolidated Financial Statements for information on the Company's exploration subsidiary.

### CURRENT GAS SUPPLY

The following tabulation shows the expected peak-day availability of gas in thousand cubic feet (Mcf) during the 1987-88 heating season:

<u>Source</u>	<u>Peak-Day Availability (Mcf)</u>	<u>Year of Contract Expiration</u>
Flow Gas		
Natural.....	135,371	1990 (a)
Company (LP).....	60,000	
	<u>195,371</u>	
Storage Gas		
Natural.....	97,153 (b)	1990-1995 (a)
Peoples Gas (Manlove).....	59,000 (c)	1990
	<u>156,153</u>	
Total expected peak-day availability....	<u>351,524 (d)</u>	

- (a) Natural Gas Pipeline Company of America (Natural) may not terminate service at the expiration of service agreements without receiving prior authorization from the FERC.
- (b) The Company has storage service withdrawals available from Natural of (1) 53,029 Mcf per day subject to maximum seasonal withdrawal of 30 times the maximum daily withdrawal under a service agreement extending to 1990, (2) 6,657 Mcf per day under a service agreement extending to 1992, (3) 4,055 Mcf per day in the peak month, which is January, under a service agreement extending to 1991, (4) 3,412 Mcf per day under a service agreement extending to 1995, and (5) 30,000 Mcf per day under a service agreement expiring in 1990.
- (c) The Company has a gas storage agreement with Peoples Gas which provides a maximum withdrawal of 59,000 Mcf of storage service per day. The agreement also makes available "needle peaking" capacity at the discretion of Peoples Gas.
- (d) See discussion of Order No. 436 and Order No. 500 under "Federal Legislation and Regulation".

ITEM 1. BUSINESS (Continued)

CURRENT GAS SUPPLY (Continued)

The Company's sources of gas supply (including gas transported for customers) in million cubic feet (MMcf) for the three fiscal years ended September 30, 1987, 1986 and 1985 are as follows:

	<u>1987</u>	<u>1986</u>	<u>1985</u>
Source:			
Natural (a)	11,330	31,625	31,802
Other Suppliers (a)	15,470	918	--
Peoples Gas - SNG (b)	--	276	841
- Other	--	944	--
Liquefied Petroleum Gas Produced	5	3	18
Customer Owned Gas - Received	4,390	17	--
Underground Storage - Net	255	(559)	(207)
Company Use, Franchise Requirements and Unaccounted for Gas	<u>(287)</u>	<u>(148)</u>	<u>(432)</u>
Total (c)	<u>31,163</u>	<u>33,076</u>	<u>32,022</u>

- (a) The Company began making significant purchases of supplies in the competitive spot market in fiscal 1987, substituting these supplies for more expensive pipeline supplies. Such purchases are made on a month-to-month basis where they produce a significant savings in gas costs. See discussion of Order No. 436 and Order No. 500 under "Federal Legislation and Regulation".
- (b) North Shore's service agreement with Peoples Gas which provided for the purchase of 10 per cent of the production of Peoples Gas' SNG plant, expired in fiscal 1986 and was not renewed.
- (c) The variation in total supply from year-to-year is due primarily to weather.

## ITEM 2. PROPERTIES

All of the principal plants and properties of the Company have been maintained in the ordinary course of business and are believed to be in satisfactory operating condition. The following is a brief description of the principal plants and operating units of the Company.

The distribution system of the Company, as of September 30, 1987, consisted of 1,736 miles of distribution mains and necessary pressure regulators, approximately 99,000 services (pipe connecting the mains with piping on the customers' premises) and approximately 110,000 meters installed on customers' premises. The Company has liquefied petroleum gasification and storage facilities. It also owns and has a substantial investment in office and service buildings, garages, repair shops and motor vehicles, together with the equipment, tools and fixtures necessary to conduct its business.

Most of the principal plants and properties of the Company, other than mains, services, meters, regulators and cushion gas in underground storage, are located on property owned in fee. Substantially all gas mains are installed in public streets, alleys and highways, or under property owned by others under grants of easements. Meters and house regulators in use and a portion of services are located on premises being served.

Substantially all of the physical properties now owned or hereafter acquired by the Company are subject to (a) the direct, first mortgage lien of the Company's Mortgage to the Continental Illinois National Bank and Trust Company of Chicago, Trustee, to secure the principal amount of the Company's outstanding First Mortgage Bonds and (b) in certain cases, other exceptions and defects which do not interfere with the use of the property.

## ITEM 3. LEGAL PROCEEDINGS

There are no material legal proceedings pending to which the Company is a party.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

## PART II

### ITEM 5. MARKET FOR THE COMPANY'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The Company is a wholly-owned subsidiary of Peoples Energy.

### ITEM 6. SELECTED FINANCIAL DATA

For fiscal years ended September 30,	1987	1986	1985	1984	1983
<b>OPERATING RESULTS (thousands)</b>					
Operating Revenues:					
Residential	\$ 81,791	\$ 96,265	\$ 99,472	\$ 98,818	\$ 85,984
Commercial	31,380	38,133	40,837	40,319	35,537
Industrial	12,211	30,409	34,052	37,765	29,845
Transportation of customer-owned gas	2,662	7	--	--	--
Other	114	944	966	1,199	1,374
Total Operating Revenues	<u>128,158</u>	<u>165,758</u>	<u>175,327</u>	<u>173,101</u>	<u>152,735</u>
Less - Gas costs	77,616	108,893	118,789	122,314	108,049
- Revenue taxes	8,591	11,094	12,026	11,598	10,541
Net Operating Revenues	<u>\$ 41,951</u>	<u>\$ 45,771</u>	<u>\$ 44,512</u>	<u>\$ 39,189</u>	<u>\$ 34,145</u>
Net Income Applicable to Common Stock	\$ 7,183	\$ 8,900	\$ 8,782	\$ 6,847	\$ 4,549
<b>GAS SOLD AND TRANSPORTED (million cubic feet)</b>					
Residential	16,670	18,161	17,209	18,323	16,378
Commercial	7,288	8,090	7,946	8,377	7,563
Industrial	2,956	6,806	6,867	6,924	6,369
Transportation of customer-owned gas	4,249	19	--	--	--
Total	<u>31,163</u>	<u>33,076</u>	<u>32,022</u>	<u>33,624</u>	<u>30,310</u>
<b>NUMBER OF CUSTOMERS (average)</b>					
Residential	99,537	96,281	94,393	93,126	92,256
Commercial	6,241	5,962	5,769	5,595	5,487
Industrial	704	717	700	695	655
Transportation	52	1	--	--	--
Total	<u>106,534</u>	<u>102,961</u>	<u>100,862</u>	<u>99,416</u>	<u>98,398</u>
<b>DEGREE DAYS</b>					
Per cent of normal (6,455)	89	105	103	111	97
<b>ASSETS (thousands)</b>					
Property, plant and equipment	\$151,020	\$138,601	\$128,767	\$121,629	\$116,888
Less-Accumulated depreciation	48,640	45,299	41,803	38,477	35,873
Net Property, Plant and Equipment	<u>\$102,380</u>	<u>\$ 93,302</u>	<u>\$ 86,964</u>	<u>\$ 83,152</u>	<u>\$ 81,015</u>
Capital expenditures - construction	\$ 14,539	\$ 10,810	\$ 8,072	\$ 6,186	\$ 6,480
Total Assets	<u>\$131,802</u>	<u>\$123,957</u>	<u>\$130,756</u>	<u>\$122,780</u>	<u>\$131,546</u>
<b>CAPITALIZATION AT YEAR END (thousands)</b>					
Common equity	\$ 47,961	\$ 44,295	\$ 41,197	\$ 39,086	\$ 37,824
Preferred stock	3,000	3,000	4,000	5,000	6,000
Long-term debt	23,525	27,625	33,082	38,494	39,936
Total	<u>\$ 74,486</u>	<u>\$ 74,920</u>	<u>\$ 78,279</u>	<u>\$ 82,580</u>	<u>\$ 83,760</u>
<b>CAPITALIZATION RATIOS AT YEAR END (per cent)</b>					
Common equity	64	59	53	47	45
Preferred stock	4	4	5	6	7
Long-term debt	32	37	42	47	48
Total	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>

The Company is a wholly-owned subsidiary of Peoples Energy; therefore, cash dividends declared per share and earnings per share are omitted.



ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Results of Operations

Net income applicable to common stock decreased by \$1.7 million in 1987, primarily due to much warmer weather than in the previous year. The increase in 1986 was mainly the result of colder weather.

Revenues for 1987 have been reduced to provide for the possibility of a refund to customers in connection with provisions of its rate schedule relating to the reduction in the maximum federal income tax rate under the Tax Reform Act of 1986. See Note (3) and Note (17) of Notes to Consolidated Financial Statements.

The Company has been experiencing significant decreases in operating revenues due, in part, to increased purchases of gas directly from producers by some of its larger customers. However, this has no overall effect on operating income since the charges for transporting the gas through the Company's distribution system provide similar margins as those for gas sales.

Weather variations affect the volumes of gas delivered for heating and, therefore, can have a significant impact on net income. The effect on net income of the major operating cost - that of gas purchased or produced - is minimized because a substantial portion of these costs is recovered from retail customers through the gas-cost recovery provision in the Company's rate schedule.

Since utility properties are reported and recovered through rates at historical cost, the potentially material effect of inflation and changing prices is not reflected in the financial statements.

A summary of significant variations in income is presented below, with explanations following:

(Thousands of dollars)	Fiscal 1987 Over 1986		Fiscal 1986 Over 1985	
	Amount	%	Amount	%
Net operating revenues*	\$(3,820)	(8.3)	\$1,259	2.8
Income taxes	(2,448)	(27.9)	(582)	(6.2)
Other income	(836)	(58.7)	(205)	(12.6)
Income deductions	(609)	(13.2)	(97)	(2.1)
Net Income Applicable to Common Stock	(1,717)	(19.3)	118	1.3

\* Operating revenues net of gas costs and revenue taxes.  
( ) Denotes red figure.

The primary reasons for the decrease in 1987 net operating revenues are warmer weather than in 1986 and the above-mentioned possibility of a refund to customers. The increase in 1986 results mainly from colder weather.

Factors contributing to the decline in income taxes include a reduction in the federal income tax rate and lower pre-tax income. The decrease in 1986 mainly reflects reduced pre-tax income.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Results of Operations (Continued)

The decrease in other income in both periods is primarily due to lower interest rates. Contributing further to the decline in 1987 was less cash available for short-term investments and less interest on amounts recoverable from customers.

Income deductions decreased in both periods reflecting less interest expense on long-term debt due to a reduction in the amount of bonds outstanding. Additionally in 1987, there was less interest on amounts refundable to customers.

Liquidity and Capital Resources

The Company has access to outside capital markets and to internal sources of funds that together should provide sufficient resources to meet capital requirements. The Company does not anticipate any changes that materially would alter its current liquidity position.

Due to the seasonal nature of gas sales, a major portion of cash collections occurs between November and April. Because of timing differences in the receipt and disbursement of cash, and the level of construction requirements, the Company may borrow on a short-term basis. Short-term borrowings are either repaid with cash from operations or refinanced on a permanent basis with debt and/or equity, depending on money-market conditions and capital structure considerations.

The Company issued \$20 million ten-year First Mortgage Bonds, 10.2% Series I, on December 1, 1987. Proceeds from the issuance will be used to retire short-term debt and for capital expenditures.

Additional bonds are issuable, upon Commission approval, subject to limitations by certain restrictive provisions of the open-end mortgage and supplements thereto. Short-term cash needs are met through borrowing arrangements with banks and/or the issuance of commercial paper. See Note (10) of Notes to Consolidated Financial Statements.

Capital expenditures for additions, replacements, and improvements to the utility plant were \$14.5 million in 1987, \$10.8 million in 1986 and \$8.1 million in 1985. Capital expenditures for fiscal 1988 are estimated to be \$17.9 million.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

	<u>Page</u>
Report of Independent Public Accountants	14
Consolidated Statements of Income for the fiscal years ended September 30, 1987, 1986 and 1985	15
Consolidated Statements of Retained Earnings for fiscal years ended September 30, 1987, 1986 and 1985	15
Consolidated Balance Sheets as of September 30, 1987 and 1986	16
Consolidated Capitalization Statements as of September 30, 1987 and 1986	17
Consolidated Statements of Changes in Financial Position for the fiscal years ended September 30, 1987, 1986 and 1985	18
Notes to Consolidated Financial Statements	19
Selected Quarterly Financial Data	28

ITEM 9. CHANGES IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND  
FINANCIAL DISCLOSURE

Not applicable.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To North Shore Gas Company:

We have examined the consolidated balance sheets and capitalization statements of North Shore Gas Company (an Illinois corporation, hereinafter referred to as the Company and a wholly-owned subsidiary of Peoples Energy Corporation) and subsidiary companies as of September 30, 1987, and 1986, and the related consolidated statements of income, retained earnings, and changes in financial position for each of the three years in the period ended September 30, 1987. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the financial statements referred to above present fairly the financial position of the Company and subsidiary companies as of September 30, 1987, and 1986, and the results of their operations and changes in financial position for each of the three years in the period ended September 30, 1987, in conformity with generally accepted accounting principles which, except for the change, with which we concur, in the method of accounting for pensions as described in Note (4) of the notes to consolidated financial statements, were applied on a consistent basis.

Our examinations were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The financial statement schedules listed in Item 14(a)2 are presented for purposes of complying with the Securities and Exchange Commission's rules and are not part of the basic financial statements. These schedules have been subjected to the auditing procedures applied in the examinations of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN & CO.

Chicago, Illinois  
November 4, 1987

North Shore Gas Company

CONSOLIDATED STATEMENTS OF INCOME  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1987	1986	1985
OPERATING REVENUES:			
Gas sales	\$125,382	\$164,807	\$174,361
Other	2,776	951	966
Total Operating Revenues	<u>128,158</u>	<u>165,758</u>	<u>175,327</u>
OPERATING EXPENSES:			
Gas costs	77,616	108,893	118,789
Operation	16,239	16,345	15,258
Maintenance	2,459	2,453	2,106
Depreciation	4,541	4,343	4,106
Taxes - Income	6,341	8,789	9,371
- State and local revenue	8,591	11,094	12,026
- Other	1,461	1,362	1,339
Total Operating Expenses	<u>117,248</u>	<u>153,279</u>	<u>162,995</u>
OPERATING INCOME	10,910	12,479	12,332
OTHER INCOME:			
Interest income	331	1,234	1,491
Allowance for funds used during construction	25	--	--
Miscellaneous	232	190	138
Total Other Income	<u>588</u>	<u>1,424</u>	<u>1,629</u>
GROSS INCOME	11,498	13,903	13,961
INCOME DEDUCTIONS:			
Interest on long-term debt	2,962	3,521	3,693
Other interest	1,032	1,080	1,005
Amortization of debt discount and expense	21	23	24
Miscellaneous	1	1	--
Total Income Deductions	<u>4,016</u>	<u>4,625</u>	<u>4,722</u>
NET INCOME	7,482	9,278	9,239
Preferred stock dividends	<u>299</u>	<u>378</u>	<u>457</u>
NET INCOME APPLICABLE TO COMMON STOCK	<u>\$ 7,183</u>	<u>\$ 8,900</u>	<u>\$ 8,782</u>

CONSOLIDATED STATEMENTS OF RETAINED EARNINGS  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1987	1986	1985
BALANCE AT BEGINNING OF YEAR	\$ 19,538	\$ 16,440	\$ 14,329
Add - Net Income	7,482	9,278	9,239
Deduct - Dividends on common stock	3,517	5,802	6,671
- Dividends on preferred stock	<u>299</u>	<u>378</u>	<u>457</u>
BALANCE AT END OF YEAR	<u>\$ 23,204</u>	<u>\$ 19,538</u>	<u>\$ 16,440</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company  
CONSOLIDATED BALANCE SHEETS  
(Thousands of Dollars)

	<u>As of September 30,</u>	
	<u>1987</u>	<u>1986</u>
<u>PROPERTIES AND OTHER ASSETS</u>		
<u>CAPITAL INVESTMENTS:</u>		
Property, plant and equipment, at original cost	\$151,020	\$138,601
Less - Accumulated depreciation	48,640	45,299
	<u>102,380</u>	<u>93,302</u>
Gas supply advances and investments	1,358	1,564
TOTAL CAPITAL INVESTMENTS	<u>103,738</u>	<u>94,866</u>
<u>CURRENT ASSETS:</u>		
Cash	596	769
Temporary cash investments, at cost that approximates market value	1,000	--
Receivables -		
Customers, net of allowance for uncollectible accounts of \$544 and \$634, respectively	4,129	5,338
Other	39	222
Materials and supplies, at average cost	1,687	1,396
Gas in storage, at last-in, first-out cost	19,054	20,136
Gas costs recoverable through rate adjustments	118	5
Prepayments	598	443
TOTAL CURRENT ASSETS	<u>27,221</u>	<u>28,309</u>
DEFERRED CHARGES	<u>843</u>	<u>782</u>
TOTAL PROPERTIES AND OTHER ASSETS	<u>\$131,802</u>	<u>\$123,957</u>
<u>CAPITALIZATION AND LIABILITIES</u>		
CAPITALIZATION (see accompanying statement)	\$ 74,486	\$ 74,920
<u>CURRENT LIABILITIES:</u>		
Interim loans	11,500	--
Accounts payable	7,203	7,503
Dividends payable on preferred stock	--	10
Customer deposits	5,081	4,819
Sinking fund payments and maturities		
Long-term debt	2,339	3,707
Redeemable cumulative preferred stock	--	1,000
Accrued taxes	(214)	1,092
Gas sales revenue refundable	9,045	9,828
Accrued interest	214	280
TOTAL CURRENT LIABILITIES	<u>35,168</u>	<u>28,239</u>
<u>RESERVES AND DEFERRED CREDITS:</u>		
Deferred income taxes - primarily accelerated depreciation	15,758	15,030
Investment tax credits being amortized over the average lives of related property	5,099	5,140
Other	1,291	628
TOTAL RESERVES AND DEFERRED CREDITS	<u>22,148</u>	<u>20,798</u>
TOTAL CAPITALIZATION AND LIABILITIES	<u>\$131,802</u>	<u>\$123,957</u>

The accompanying notes are an integral part of these statements.

( ) Denotes red figure.

North Shore Gas Company  
CONSOLIDATED CAPITALIZATION STATEMENTS  
(Thousands of Dollars)

	<u>As of September 30,</u>	
	<u>1987</u>	<u>1986</u>
COMMON STOCKHOLDER'S EQUITY:		
Common stock, without par value		
Authorized 5,000,000 shares,		
Outstanding 3,625,887 shares	\$ 24,757	\$ 24,757
Retained earnings (see accompanying statement)	<u>23,204</u>	<u>19,538</u>
TOTAL COMMON STOCKHOLDER'S EQUITY	47,961	44,295
REDEEMABLE CUMULATIVE PREFERRED STOCK:		
Exclusive of sinking fund payments, due within one year		
Authorized 190,000 and 200,000 shares, respectively,		
par value \$100		
9% Series, 30,000 shares outstanding	<u>3,000</u>	<u>3,000</u>
TOTAL REDEEMABLE CUMULATIVE PREFERRED STOCK	3,000	3,000
LONG-TERM DEBT:		
Exclusive of sinking fund payments and maturities,		
due within one year		
First Mortgage Bonds -		
9-1/2% Series E, due February 1, 1995	6,375	6,625
8-3/8% Series F, due October 1, 1998	7,250	7,500
8-3/8% Series G, due February 15, 1992	2,400	3,000
12% Series H, due September 15, 1995	<u>7,500</u>	<u>10,500</u>
TOTAL LONG-TERM DEBT	<u>23,525</u>	<u>27,625</u>
TOTAL CAPITALIZATION	<u>\$ 74,486</u>	<u>\$ 74,920</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1987	1986	1985
FUNDS PROVIDED:			
Net income	\$ 7,482	\$ 9,278	\$ 9,239
Add - Principal items not requiring current outlay of funds			
Depreciation	4,541	4,343	4,106
Deferred income taxes - primarily accelerated depreciation	838	1,264	1,353
Deferred investment tax credits - net	(168)	13	430
TOTAL FUNDS PROVIDED FROM OPERATIONS	12,693	14,898	15,128
Change in deferred credits - possible refund to customers	678	--	--
Other	1,067	--	591
TOTAL FUNDS PROVIDED	<u>\$ 14,438</u>	<u>\$ 14,898</u>	<u>\$15,719</u>
FUNDS APPLIED:			
Capital expenditures - construction	\$ 14,539	\$ 10,810	\$ 8,072
Reduction of:			
Long-term debt	5,468	6,662	1,444
Preferred stock	1,000	1,000	1,000
Dividends on common stock	3,517	5,802	6,671
Dividends on preferred stock	299	378	457
Decrease in working capital	(10,385)	(10,333)	(1,925)
Other	--	579	--
TOTAL FUNDS APPLIED	<u>\$ 14,438</u>	<u>\$ 14,898</u>	<u>\$15,719</u>
INCREASE (DECREASE) IN WORKING CAPITAL, EXCLUSIVE OF CURRENT MATURITIES OF LONG-TERM DEBT AND SINKING FUND PAYMENTS, BY COMPONENT:			
Cash and temporary cash investments	\$ 827	\$(12,823)	\$ 3,847
Receivables and payables - net	(1,082)	2,016	850
Interim loans	(11,500)	--	--
Gas in storage	(1,082)	1,180	116
Rate adjustments refundable or recoverable	896	(1,353)	(3,947)
Accrued taxes	1,306	(103)	(1,990)
Customer deposits	(262)	355	(322)
Materials and supplies	291	73	(576)
Other	221	322	97
DECREASE IN WORKING CAPITAL	<u>\$(10,385)</u>	<u>\$(10,333)</u>	<u>\$(1,925)</u>

The accompanying notes are an integral part of these statements.

( ) Denotes red figure.



North Shore Gas Company

STATEMENT OF MANAGEMENT

These financial statements were prepared by management, which is responsible for their integrity and objectivity. The statements are in conformity with generally accepted accounting principles and, as such, reflect judgments made by management.

Based upon the Company's accounting and internal control systems, along with ongoing internal audit programs, management believes that the accounting records are reliable for the purpose of preparing financial statements, and assets are appropriately safeguarded against loss from unauthorized use.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) SIGNIFICANT ACCOUNTING POLICIES

a. Principles of Consolidation

All subsidiaries of the Company are included in the consolidated financial statements. All significant intercompany transactions have been eliminated in consolidation. Certain items previously reported for years prior to 1987 have been reclassified to conform with the current-year presentation.

b. Property, Plant and Equipment

Property, plant and equipment is stated at original cost and includes appropriate amounts of payroll taxes, employee-benefit costs, administrative costs, and an allowance for funds used during construction.

c. Allowance for Funds Used During Construction

The assumed cost of all funds used to finance substantial and lengthy construction is capitalized as a cost element of Utility Plant, with an offsetting credit to Other Income. Under established regulatory practices, the Company is permitted to include in its rates a fair return on, and the recovery of, these capitalized costs by including them in rate base and in the provision for depreciation.

The effect on fiscal 1987 net income of the allowance for funds used during construction is immaterial. There was no allowance for funds used during construction in fiscal years 1986 and 1985.

d. Maintenance and Depreciation

It is the practice of the Company to charge to maintenance the cost of repairs, renewals, and improvements amounting to less than retirement units of property. When depreciable property is retired, its original cost is charged to the accumulated provision for depreciation.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

d. Maintenance and Depreciation (Continued)

The provision for depreciation substantially reflects the systematic amortization of the original cost of depreciable property over the estimated useful lives on the straight-line method. Additionally, actual dismantling cost, net of salvage, is included in the provision for depreciation in the month incurred. The amounts provided are designed to cover not only losses due to wear and tear that are not restored by maintenance, but also losses due to obsolescence and inadequacy.

The provision for depreciation, expressed as an annual percentage of original cost of depreciable property, approximated 3.6%, 3.7% and 3.7% for fiscal years 1987, 1986 and 1985, respectively.

e. Recovery of Gas Costs

Under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or a current asset (with a contra entry to gas costs), and the fiscal year-end balance is amortized over the 12-month period beginning the following January 1.

f. Gas in Storage

Storage injections are priced at the fiscal-year average of demand and commodity costs of natural gas purchased. Withdrawals from storage are priced on the last-in, first-out (LIFO) method. The estimated current replacement cost of gas in inventory, at September 30, 1987, and 1986, exceeded the LIFO cost by approximately \$25 million and \$30 million, respectively.

g. Taxes

For federal and Illinois income-tax purposes, for periods prior to January 1, 1981, the Company adopted liberalized methods of computing depreciation on property additions after December 31, 1953, and the Asset Depreciation Range (ADR) system on property additions after December 31, 1970. For periods after December 31, 1980, the Company utilized the Accelerated Cost Recovery System (ACRS), and the Modified Accelerated Cost Recovery System (MACRS) on property additions after December 31, 1986.

Deferred income taxes for the difference between tax depreciation computed on these methods and straight-line depreciation are charged to income and credited to accumulated deferred income taxes. This account is charged when liberalized, ADR, ACRS, or MACRS tax depreciation becomes less than straight-line depreciation.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

g. Taxes (Continued)

The investment tax credits have been deferred and are being amortized through credits to income over the book lives of related property. The Tax Reform Act of 1986, signed into law on October 22, 1986, repeals the investment tax credit for property placed in service after December 31, 1985, subject to certain transition rules.

At September 30, 1987, the cumulative net amount of timing differences for which deferred income taxes have been over provided is approximately \$.7 million.

The preceding deferred-tax and tax-credit accounting conforms with regulations of the Commission.

h. Accounting for Pensions

Effective October 1, 1986, the Company adopted the provisions of FASB Statement No. 87, "Employers' Accounting for Pensions." The consolidated pension expense for fiscal 1987 was \$.8 million as compared to \$1.3 million for fiscal 1986. The primary reason for this difference was the implementation of FASB Statement No. 87.

i. Illinois Residential Affordable Payment Program (IRAPP)

Under IRAPP, the Company is prohibited from discontinuing gas service to any participating customer who pays the monthly obligation required by IRAPP (the monthly obligation). For the period December 1 through April 30, the monthly obligation is 8 per cent of the customer's income and for the period May 1 through November 30 that obligation is the greater of 8 per cent of the customer's income or the full amount of the customer's current bill calculated under tariff provisions (the current bill). The difference between the current bill (excluding for winter months, charges for usage exceeding the customer's average usage) and the monthly obligation is referred to as "shortfall."

The Commission has ruled that IRAPP participants are not at any time required to pay for the shortfall. Therefore, accumulated shortfall is excluded from gas sales and is reflected in deferred credits with a corresponding amount in deferred charges. Amounts representing shortfall are recognized as gas sales when recovered from sources other than IRAPP participants (such as governmental assistance programs). At September 30, 1987, the accumulated shortfall reflected in the deferred accounts was \$54,000. The Company cannot reasonably determine at this time the future impact of accumulated shortfall not recovered from sources other than IRAPP participants.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(2) COVENANTS REGARDING RETAINED EARNINGS

The Company's Indenture relating to the First Mortgage Bonds and the Stock Purchase Agreements relating to the Cumulative Preferred Stock contain provisions and covenants restricting the payment of cash dividends and the purchase or redemption of capital stock. At September 30, 1987, such restrictions amounted to \$4.4 million out of total retained earnings of \$23.2 million.

(3) RATES AND REGULATION

The Company filed with the Commission a new rider to its rate schedule to provide for recording deferred credits relating to the reduction in the maximum federal income tax rate for corporate taxpayers under the Tax Reform Act of 1986. The Company filed its rider under a special procedure established for all Illinois utilities for this purpose by order of the Commission. The rider became effective on March 1, 1987. The new rider provides for recording each month in a deferred credit account an amount equal to 3.6 per cent of the Company's base revenues.

The rider provides that it will remain in effect until the Commission has made a review of the Company's operating income, including all aspects of the Tax Reform Act of 1986, to determine whether a refund and/or a prospective rate reduction is warranted. The Company's rider also provides that a refund to customers would be due only if the Commission finds after hearing and so orders that a reduction in rates would have been proper as of the effective date of the rider.

The Company has entered into discussions with the staff of the Commission and other parties regarding the propriety of a filing by the Company to seek Commission approval of the termination of its rider, with a refund from the deferred credits recorded thereunder and/or a prospective reduction in rates to reflect, among other things, a lower cost of capital and reduced level of federal income taxes from those reflected in its most recent rate order. If these discussions do not result in a filing for a proposed refund and/or prospective rate reduction, the Commission may commence an investigation of the Company's rates.

The Company cannot determine at this time whether the discussions, as described above, or any Commission proceeding that may follow such discussions, will result in a refund and/or rate reduction that will have a material adverse financial effect on the Company. However, reflecting the possibility of a refund to customers for all or part of the deferred credits recorded under its rider, the Company has reduced its revenues for fiscal 1987 by \$678,000, the amount of deferred credits at September 30, 1987.

See Note (17) of Notes to Consolidated Financial Statements for Event Subsequent to Date of Financial Statements.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(4) PENSION PLANS AND POST-RETIREMENT BENEFITS

The Company participates in two defined benefit pension plans covering substantially all employees. The plans provide pension benefits that generally are based on an employee's length of service, compensation during the five years preceding retirement, and social security benefits. The Company makes annual contributions to the plans based upon actuarial determinations and in consideration of tax regulations and funding requirements under federal law.

The Company adopted Financial Accounting Standards Board Statement No. 87 effective October 1, 1986, which required a change in the actuarial cost method and certain other actuarial assumptions used in determining pension cost. These changes had the effect of reducing fiscal 1987 pension cost by \$.4 million compared to the previous method. Net pension cost for fiscal 1987 includes the following components:

	<u>(Millions)</u>
Service Cost	\$ .7
Interest Cost	1.7
Actual Return on Plan Assets	(4.8)
Net Amortization and Deferral	<u>3.2</u>
Net Pension Cost	<u>\$ .8</u>

The calculation of pension cost assumed a weighted average discount rate of 6.9%, a 5.5% rate of compensation increase, and a 6.5% long-term rate of return on assets. In accordance with the provisions of FASB No. 87, pension expense has not been restated for prior years. Pension expense for fiscal years 1986 and 1985 was \$1.3 million and \$1.2 million, respectively.

The funded status of the Company's pension plans at September 30, 1987 was as follows:

	<u>(Millions)</u>
Actuarial present value of plan benefits:	
Vested	\$15.8
Nonvested	<u>1.9</u>
Accumulated benefit obligation	17.7
Effect of projected future compensation increases	<u>6.5</u>
Projected benefit obligation	24.2
Plan assets at market value	<u>29.1</u>
Plan assets in excess of projected benefit obligation	<u>\$ 4.9*</u>
* Comprised of:	
Effect of changes in assumptions and difference between actual and estimated experience	\$ 4.4
Unrecognized transition asset	<u>.5</u>
	<u>\$ 4.9</u>

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(4) PENSION PLANS AND POST-RETIREMENT BENEFITS (Continued)

The projected benefit obligation was determined using a weighted average discount rate of 7.4% and assumed future compensation increases of 5.5%. Plan assets consist primarily of marketable equity and fixed income securities.

In addition to providing pension benefits, the Company provides certain health-care and life insurance benefits for retired employees. Substantially all employees may become eligible for such benefit coverage if they reach retirement age while working for the Company. The costs of providing these benefits are recognized as an expense during the period in which the costs are incurred. Such costs during fiscal years 1987, 1986, and 1985 were \$186,000, \$154,000 and \$147,000, respectively.

(5) TAX MATTERS

Provision for Income Taxes For fiscal years ended September 30,	1987	1986	1985
	(000' s)		
Current:			
Federal	\$ 4,876	\$ 6,497	\$ 6,554
State	790	1,015	1,034
Total current income taxes	<u>5,666</u>	<u>7,512</u>	<u>7,588</u>
Deferred, net - Primarily accelerated depreciation			
Federal	736	1,102	1,181
State	<u>102</u>	<u>162</u>	<u>172</u>
Total deferred income taxes - Primarily accelerated depreciation	<u>838</u>	<u>1,264</u>	<u>1,353</u>
Investment tax credits - net:			
Federal	(248)	(21)	395
State	<u>80</u>	<u>34</u>	<u>35</u>
Total investment tax credits - net	<u>(168)</u>	<u>13</u>	<u>430</u>
Total provision for income taxes	6,336	8,789	9,371
Less - Included in other income or operation expense	<u>(5)</u>	<u>—</u>	<u>—</u>
Included in operating expenses as taxes - income	<u>\$ 6,341</u>	<u>\$ 8,789</u>	<u>\$ 9,371</u>

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(5) TAX MATTERS (Continued)

The following is a reconciliation between the computed federal income tax expense (tax rates of 43 per cent in 1987, and 46 per cent in 1986 and 1985, times pre-tax income) and the total provision for federal income tax expenses:

For fiscal years ended September 30,	1987		1986		1985	
	Amount (000's)	Per Cent of Pre-tax Income	Amount (000's)	Per Cent of Pre-tax Income	Amount (000's)	Per Cent of Pre-tax Income
Computed federal income tax expense	\$5,524	43.0	\$7,754	46.0	\$7,990	46.0
Amortization of investment tax credit	(248)	(1.9)	(249)	(1.5)	(241)	(1.4)
Out of period items at different tax rates	53	0.4	—	—	—	—
Book depreciation over depreciation used in tax provision	73	0.6	75	0.5	78	0.5
Other	<u>(38)</u>	<u>(0.3)</u>	<u>(2)</u>	<u>—</u>	<u>303</u>	<u>1.7</u>
Total provision for federal income taxes	<u>\$5,364</u>	<u>41.8</u>	<u>\$7,578</u>	<u>45.0</u>	<u>\$8,130</u>	<u>46.8</u>

( ) Denotes red figure.

Tax returns for 1980 through 1982 have been audited by the Internal Revenue Service and a tax deficiency of approximately \$508,000 has been proposed. Issues are being contested, and the potential impact on net income is not believed to be material, since the issues consist of income tax provision timing differences.

Tax returns for 1983 and 1984 have been audited by the Internal Revenue Service and a tax deficiency of approximately \$933,000 has been proposed. Issues are being contested, and the potential impact on net income is not believed to be material, since the issues consist of income tax provision timing differences.

Tax returns for 1985 and 1986 are currently under audit by the Internal Revenue Service.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(6) DEFERRED CHARGES

	<u>As of September 30,</u>	
	<u>1987</u>	<u>1986</u>
	<u>(000's)</u>	
Interest on gas sales revenue refundable	\$381	\$463
Debt expense being amortized over the lives of outstanding issues	152	174
Energy Conservation Plan expenses	95	110
Unamortized Discount - Notes payable	62	--
IRAPP shortfall sales	54	--
Other	99	35
	<u>\$843</u>	<u>\$782</u>

(7) REDEEMABLE CUMULATIVE PREFERRED STOCK

	<u>9.0% Series</u>
Year of issue	1980
Shares outstanding	30,000
Involuntary liquidation preference (000's)	\$ 3,000
Annual dividends per share	\$ 9.00
Redemption options:	
Currently effective redemption price per share	(a)
Redemption price per share decreases annually to issue price by (year)	(a)
Redemption through certain refunding operations not permitted prior to (year)	1990

---

(a) Not currently redeemable at the option of the Company.

(8) COMMON STOCK

No common stock was issued during the fiscal years 1985 through 1987.

(9) SINKING FUND REQUIREMENTS

Sinking fund requirements of preferred stock outstanding at September 30, 1987, are \$3.0 million for fiscal year 1991. There are no sinking fund requirements for fiscal years 1988 through 1990 and 1992.

Sinking fund requirements and maturities of long-term debt outstanding at September 30, 1987, for fiscal years 1988 through 1992 are \$2.3 million for 1988 and \$2.4 million for 1989 and \$2.6 million each year for 1990 through 1992.



North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(10) SHORT-TERM BORROWING AND COMPENSATING BALANCES

Short-term cash needs of the Company are met through bank loans and/or the issuance of commercial paper. The outstanding total amount of these borrowings cannot at any time exceed total bank credit then in effect.

During fiscal 1987, Peoples Gas maintained \$63 million in bank credit through an irrevocable revolving credit agreement. This amount has been secured for fiscal 1988 and 1989. The Company may borrow up to \$15 million.

Payment for the revolving credit agreement with the banks is through compensating balances and/or fees. There were no legal restrictions on withdrawal of compensating balances.

For additional information on short-term borrowings, see Schedule IX.

(11) CAPITAL COMMITMENTS

Total contract and purchase order construction commitments of the Company at September 30, 1987, amounted to approximately \$2.1 million.

(12) ASSETS SUBJECT TO LIEN

The Indenture of Mortgage, dated April 1, 1955, as supplemented, securing the First Mortgage Bonds issued by the Company, constitutes a direct, first-mortgage lien on substantially all property owned by the Company.

(13) EXPLORATION SUBSIDIARY

North Shore Exploration Company, a wholly-owned subsidiary of the Company, was formed in 1973 to engage, directly or indirectly, in lease-acquisition and exploration and development programs. The exploration unit has made investments totaling \$4.1 million and through September 30, 1987, has amortized \$3.6 million. The Company is allowed by the Commission to include such investments in its rate base and treat any profits or losses as utility transactions.

(14) TEMPORARY CASH INVESTMENTS

Temporary cash investments at September 30, 1987, consisted of Eurodollar Deposits maturing October 1, 1987.

(15) LEGAL PROCEEDINGS

There are no material legal proceedings pending to which the Company is a party.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(16) SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	<u>Operating Revenues</u>	<u>Operating Income</u> (000' s)	<u>Net Income Applicable to Common Stock</u>
First Quarter			
1987	\$ 37,092	\$ 3,575	\$ 2,411
1986	45,575	3,738	2,667
Second Quarter			
1987	54,782	6,379	5,358
1986	73,719	7,259	6,295
Third Quarter			
1987	25,326	1,662	888
1986	30,101	1,580	968
Fourth Quarter			
1987	10,958	(706)	(1,474)
1986	16,363	(98)	(1,030)
Fiscal Year			
1987	128,158	10,910	7,183
1986	165,758	12,479	8,900

( ) Denotes red figure.

(17) EVENT SUBSEQUENT TO DATE OF FINANCIAL STATEMENTS

Reference is made to Note (3), "Rates and Regulation", of Notes to Consolidated Financial Statements.

On December 22, 1987, the Illinois Commerce Commission approved the filing made by the Company to make effective in January, 1988 a one-time refund and a prospective rate reduction. North Shore will refund \$1.1 million and reduce rates to reflect a reduction in annual operating revenues (excluding additional charges for revenue taxes) of \$2.9 million. The rider to the Company's rate schedule, which became effective in March, providing for recording of deferred credits relating to the reduction in the maximum federal income tax rate, will be terminated.

The Company's refund and rate reduction is the result of a dollar settlement agreement with several parties regarding the Company's rates without agreement on the elements of cost of service, cost of common equity and overall rate of return.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY

IDENTIFICATION OF DIRECTORS

<u>Name, Principal Occupation and Other Directorships</u>	<u>Age at 12-02-87</u>	<u>Company Directorship Since</u>
J. Bruce Hasch Executive Vice President of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	49	1986
James Hinchliff Vice President and General Counsel of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas.	47	1985
Donald G. Holm Vice President, Secretary and Treasurer of the Company and Peoples Gas; Vice President, Controller, Secretary and Treasurer of Peoples Energy; Director of Peoples Gas.	60	1982
Richard E. Terry President and Chief Operating Officer of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	50	1982
Eugene A. Tracy Chairman of the Board and Chief Executive Officer of the Company, Peoples Energy and Peoples Gas; Director of LaSalle National Bank.	59	1978

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY (Continued)

IDENTIFICATION OF EXECUTIVE OFFICERS

	<u>Position at December 2, 1987</u>	<u>Age at 12-02-87</u>	<u>Position Held Since</u>
Patrick J. Doyle	Vice President	50	1985
J. Bruce Hasch	Executive Vice President	49	1985
James Hinchliff	Vice President and General Counsel	47	1984
Donald G. Holm	Vice President, Secretary and Treasurer	60	1981
John A. Lawrisuk	Vice President	59	1981
Ruel F. Lehman, Jr.	Vice President	64	1975
John F. Mooney	Vice President	53	1987
Michael S. Reeves	Executive Vice President	52	1987
Richard E. Terry	President and Chief Operating Officer	50	1987
Eugene A. Tracy	Chairman of the Board and Chief Executive Officer	59	1981

Directors and executive officers of the Company were elected to serve for a term of one year or until their successors are duly elected and qualified.

There are no family relationships between directors and executive officers of the Company.

All of the directors and executive officers of the Company have been continuously employed by the Company and/or its affiliates in various capacities for at least 10 years.

## ITEM 11. EXECUTIVE COMPENSATION

The executive officers of the Company serve both the Company and its affiliate Peoples Gas. Remuneration is paid by Peoples Gas with appropriate amounts billed to the Company for the time such officers serve North Shore. The Company was billed \$327,533 for the services of these officers during fiscal 1987, including approximately \$63,000 for the services of Mr. Tracy. No other executive officer's cash remuneration for service to North Shore exceeded \$60,000. Information regarding executive compensation paid by Peoples Gas and its affiliates to Peoples Gas officers is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1987.

### Compensation of Directors

All directors of the Company were officers of the Company who received no compensation for serving as directors.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

### SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

As of November 30, 1987, voting securities of the Company were owned as follows:

<u>Name and Address</u>	<u>Type of Ownership</u>	<u>Number of Shares Owned</u>	<u>Per Cent of Class</u>
<u>Common Stock without par value</u>			
Peoples Energy Corporation 122 South Michigan Avenue Chicago, Illinois 60603	Owned Both of Record and Beneficially	<u>3,625,887</u>	<u>100%</u>
<u>Redeemable Cumulative Preferred Stock, \$100 Par Value</u>			
GMAC Commercial Corporation General Motors Building 3044 West Grand Boulevard Detroit, Michigan 48202	Owned Both of Record and Beneficially	<u>30,000</u>	<u>100%</u>

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT (Continued)

SECURITY OWNERSHIP OF MANAGEMENT

No equity securities of the Company are beneficially owned directly or indirectly by any director or officer of the Company.

Information regarding Common Stock, without par value, of Peoples Energy beneficially owned directly or indirectly by directors and executive officers of the Company is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1987.

CHANGES IN CONTROL

None.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

None.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

	<u>Page</u>
(a) 1. Financial Statements:	
See Part II, Item 8.	13
2. Financial Statement Schedules:	
<u>Schedule</u> <u>Number</u>	
V Property, Plant and Equipment at Original Cost	34
VI Accumulated Provision for Depreciation of Property, Plant and Equipment	36
VIII Valuation and Qualifying Accounts	37
IX Short-Term Borrowings	39
X Supplementary Income Statement Information	40
3. Exhibits:	
See Exhibit Index on page 42.	
(b) Reports on Form 8-K filed during the final quarter of fiscal year 1987:	
None.	

North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 1 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<u>Fiscal Year Ended September 30, 1987</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,843	\$ 18	\$ 1	\$ (10)	\$ 3,850
Storage plant	7,271	213	--	--	7,484
Distribution plant	116,828	13,547	666	201	129,910
General plant	7,936	1,057	812 (a)	(201)	7,980
Construction work in progress	1,392	(321)	--	--	1,071
Gas stored underground - Noncurrent	701	24	--	--	725
Total public utility facilities	137,971	14,538	1,479	(10) (c)	151,020
Nonutility property	630	--	640	10	--
Total property, plant and equipment, at original cost	<u>\$138,601</u>	<u>\$ 14,538</u>	<u>\$ 2,119 (b)</u>	<u>\$ --</u>	<u>\$151,020</u>
<u>Fiscal Year Ended September 30, 1986</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,798	\$ 45	\$ --	\$ --	\$ 3,843
Storage plant	6,793	478	--	--	7,271
Distribution plant	108,633	8,922	727	--	116,828
General plant	7,087	1,098	249	--	7,936
Construction work in progress	1,178	214	--	--	1,392
Gas stored underground - Noncurrent	648	53	--	--	701
Total public utility facilities	128,137	10,810	976	--	137,971
Nonutility property	630	--	--	--	630
Total property, plant and equipment, at original cost	<u>\$128,767</u>	<u>\$ 10,810</u>	<u>\$ 976 (b)</u>	<u>\$ --</u>	<u>\$138,601</u>



North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 2 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance</u> <u>at beginning</u> <u>of period</u>	<u>Additions</u> <u>at cost</u>	<u>Retirements</u>	<u>Transfers</u> <u>between</u> <u>accounts</u>	<u>Balance</u> <u>at end of</u> <u>period</u>
<u>Fiscal Year Ended September 30, 1985</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,784	\$ 14	\$ --	\$ --	\$ 3,798
Storage plant	6,254	539	--	--	6,793
Distribution plant	102,830	6,385	582	--	108,633
General plant	6,791	648	352	--	7,087
Construction work in progress	752	426	--	--	1,178
Gas stored underground - Noncurrent	<u>588</u>	<u>60</u>	<u>--</u>	<u>--</u>	<u>648</u>
Total public utility facilities	120,999	8,072	934	--	128,137
Nonutility property	<u>630</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>630</u>
Total property, plant and equipment, at original cost	<u>\$121,629</u>	<u>\$ 8,072</u>	<u>\$ 934 (b)</u>	<u>\$ --</u>	<u>\$128,767</u>

( ) Denotes red figure.

Notes: (a) Includes \$261,000 applicable to a change in minimum capitalization from \$250 to \$500.

(b) Represents:

	<u>1987</u>	<u>1986</u>	<u>1985</u>
Retirements charged to accumulated provision for depreciation Schedule (VI)	\$1,479	\$976	\$934
Cost of land retired at Peterson Road	640	--	--
	<u>\$2,119</u>	<u>\$976</u>	<u>\$934</u>

(c) Represents the transfer of Peterson Road land to Nonutility property.

## North Shore Gas Company and Subsidiary Companies

## ACCUMULATED PROVISION FOR DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

(000's)

Column A	Column B	Column C		Column D			Column E	Column F
Description	Balance at beginning of period	Additions charged to costs and expenses (a) Depreciation expense	Clearing accounts	Retirement of property at cost	Deduct retirements Cost of dismantling	Stores and miscellaneous (salvage)	Other changes	Balance at end of period
<u>Fiscal Year Ended September 30, 1987</u>								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 2,132	\$ 130	\$ --	\$ 1	\$ --	\$ --	\$ --	\$ 2,261
Storage plant	1,805	253	--	--	--	--	--	2,058
Distribution plant	38,487	3,934	--	666	198	(2)	77	41,636
General plant	2,875	224	389	812 (b)	--	(73)	(64)	2,685
Total accumulation provision for depreciation	<u>\$45,299</u>	<u>\$4,541</u>	<u>\$389</u>	<u>\$1,479</u>	<u>\$198</u>	<u>\$ (75)</u>	<u>\$ 12 (c)</u>	<u>\$48,640</u>
<u>Fiscal Year Ended September 30, 1986</u>								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 2,002	\$ 130	\$ --	\$ --	\$ --	\$ --	\$ --	\$ 2,132
Storage plant	1,562	243	--	--	--	--	--	1,805
Distribution plant	35,733	3,744	--	727	271	(8)	--	38,487
General plant	2,506	226	376	249	13	(29)	--	2,875
Total accumulation provision for depreciation	<u>\$41,803</u>	<u>\$4,343</u>	<u>\$376</u>	<u>\$976</u>	<u>\$284</u>	<u>\$ (37)</u>	<u>\$ --</u>	<u>\$45,299</u>
<u>Fiscal Year Ended September 30, 1985</u>								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 1,870	\$ 132	\$ --	\$ --	\$ --	\$ --	\$ --	\$ 2,002
Storage plant	1,336	226	--	--	--	--	--	1,562
Distribution plant	32,999	3,539	--	582	245	(12)	10	35,733
General plant	2,272	209	337	352	8	(48)	--	2,506
Total accumulation provision for depreciation	<u>\$38,477</u>	<u>\$4,106</u>	<u>\$337</u>	<u>\$934</u>	<u>\$253</u>	<u>\$ (60)</u>	<u>\$ 10 (c)</u>	<u>\$41,803</u>

( ) Denotes red figure.

Notes: (a) Reference is made in Note (1) of the notes to consolidated financial statements with respect to the basis for the provision for depreciation.

(b) Includes \$261,000 applicable to a change in minimum capitalization from \$250 to \$500.

(c) Represents the following:

	1987	1985
Accumulated provision for depreciation applicable to property acquired	\$ 2	\$ --
Proceeds from sale of property	11	10
	<u>\$13</u>	<u>\$10</u>

North Shore Gas Company and Subsidiary Companies

Schedule VIII  
Page 1 of 2

VALUATION AND QUALIFYING ACCOUNTS  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance</u> <u>at beginning</u> <u>of period</u>	<u>Additions</u> <u>Charged</u> <u>to costs</u> <u>and</u> <u>expenses</u>	<u>Deductions</u> <u>Charges for the</u> <u>purpose for which the</u> <u>reserves or deferred</u> <u>credits were created</u>	<u>Balance</u> <u>at end of</u> <u>period</u>
<u>For Fiscal Year Ended September 30, 1987</u>				
RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 634</u>	<u>\$ 903</u>	<u>\$ 993</u>	<u>\$ 544</u>
RESERVES (not deducted from assets in balance sheet) AND				
DEFERRED CREDITS:				
Injuries and damages	\$ --	\$ 72	\$ 72	\$ --
Pensions	26	2	4	24
Possible refund to customers	--	678	--	678
IRAPP Shortfall Sales	(5)	157	98	54
Other	<u>607</u>	<u>1,324</u>	<u>1,396</u>	<u>535</u>
Total	<u>\$ 628</u>	<u>\$2,233</u>	<u>\$1,570</u>	<u>\$1,291</u>

For Fiscal Year Ended September 30, 1986

RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 714</u>	<u>\$ 991</u>	<u>\$1,071</u>	<u>\$ 634</u>
RESERVES (not deducted from assets in balance sheet) AND				
DEFERRED CREDITS:				
Injuries and damages	\$ --	\$ 227	\$ 227	\$ --
Pensions	29	3	6	26
IRAPP Shortfall Sales	--	--	5	(5)
Other	<u>739</u>	<u>544</u>	<u>676</u>	<u>607</u>
Total	<u>\$ 768</u>	<u>\$ 774</u>	<u>\$ 914</u>	<u>\$ 628</u>

North Shore Gas Company and Subsidiary Companies

Schedule VIII  
Page 2 of 2

VALUATION AND QUALIFYING ACCOUNTS  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance</u> <u>at beginning</u> <u>of period</u>	<u>Additions</u> <u>Charges</u> <u>to costs</u> <u>and</u> <u>expenses</u>	<u>Deductions</u> <u>Charges for the</u> <u>purpose for which the</u> <u>reserves or deferred</u> <u>credits were created</u>	<u>Balance</u> <u>at end of</u> <u>period</u>

For Fiscal Year Ended September 30, 1985

RESERVES (deducted from assets in balance sheet):

Uncollectible items	<u>\$ 662</u>	<u>\$ 786</u>	<u>\$ 734</u>	<u>\$ 714</u>
---------------------	---------------	---------------	---------------	---------------

RESERVES (not deducted from assets in balance sheet) AND

DEFERRED CREDITS:

Injuries and damages	\$ --	\$ 33	\$ 33	\$ --
Pensions	32	6	9	29
Other	<u>540</u>	<u>785</u>	<u>586</u>	<u>739</u>
Total	<u>\$ 572</u>	<u>\$ 824</u>	<u>\$ 628</u>	<u>\$ 768</u>

North Shore Gas Company and Subsidiary CompaniesSHORT-TERM BORROWINGS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E (a)</u>	<u>Column F (b)</u>
<u>Category of Aggregate</u> <u>Short-Term Borrowings</u>	<u>Balance at</u> <u>End of Period</u>	<u>Weighted</u> <u>Average</u> <u>Interest Rate</u>	<u>Maximum Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Average Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Weighted Average</u> <u>Interest Rate</u> <u>During the Period</u>
<u>Fiscal Year Ended September 30, 1987</u>					
Commercial Paper	\$11,500	7.17%	\$11,500	\$1,726	6.87%
<u>Fiscal Year Ended September 30, 1985</u>					
Commercial Paper	\$ --	--	\$ 5,000	\$ 83	8.31%

- (a) Computed by multiplying the amounts outstanding by the days outstanding and dividing the results by the number of days used in accordance with the loan agreement.
- (b) Computed by dividing the applicable interest expense by the average amount outstanding during the period.

There were no short-term borrowings in fiscal 1986.

North Shore Gas Company and Subsidiary CompaniesSUPPLEMENTARY INCOME STATEMENT INFORMATION

Maintenance, depreciation, royalties, advertising costs and research and development costs, other than those specifically disclosed in the Consolidated Statements of Income, are not significant.

Significant taxes, other than taxes on income, including those charged to clearing and other accounts, are summarized as follows:

	<u>Fiscal Years Ended September 30,</u>		
	<u>1987</u>	<u>1986</u>	<u>1985</u>
		(000's)	
Real estate, invested capital, personal property, state capital stock and state franchise	\$ 945	\$ 927	\$ 910
Illinois public utility	5,322	6,800	7,394
Municipal public utility	3,176	4,173	4,501
Social security	712	614	577
Other	<u>308</u>	<u>311</u>	<u>248</u>
Total	<u>\$ 10,463</u>	<u>\$ 12,825</u>	<u>\$ 13,630</u>

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NORTH SHORE GAS COMPANY

Date: December 23, 1987

By: E. A. TRACY  
E. A. Tracy  
Chairman of the Board and Chief  
Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on December 23, 1987.

<u>E. A. TRACY</u> E. A. Tracy	Chairman of the Board and Chief Executive Officer and Director (Principal Executive Officer)
<u>D. G. HOLM</u> D. G. Holm	Vice President, Secretary and Treasurer and Director (Principal Financial and Accounting Officer)
<u>J. B. HASCH</u> J. B. Hasch	Director
<u>JAMES HINCHLIFF</u> James Hinchliff	Director
<u>RICHARD E. TERRY</u> Richard E. Terry	Director

North Shore Gas Company and Subsidiary Companies

EXHIBIT INDEX

- (a) The exhibits listed below are filed herewith and made a part thereof:

<u>Exhibit Number</u>	<u>Description of Document</u>	<u>Page Number</u>
3-a	Amendment to the Articles of Incorporation of the Registrant, dated April 13, 1987.	43
3-b	Articles of Incorporation, as last amended.	45
3-c	Amendment to the By-Laws of the Registrant, dated June 1, 1987.	99
3-d	By-Laws, as last amended.	100
4	Ninth Supplemental Indenture dated as of December 1, 1987	120

- (b) Exhibits listed below have been filed heretofore with the Securities and Exchange Commission pursuant to the Securities Act of 1933, as amended, and/or the Securities Exchange Act of 1934, as amended, and are incorporated herein by reference. The file number and exhibit number of each such exhibit are stated in the description of such exhibits.

Exhibit  
Number

Description of Document

- |     |   |
|-----|---|
| 4-a | Indenture, dated as of April 1, 1955, from the Company to Continental Illinois National Bank and Trust Company of Chicago as Trustee; Third Supplemental Indenture, dated as of December 20, 1963 (North Shore-File No. 2-35965, Exhibit 4-1); Fifth Supplemental Indenture, dated as of February 1, 1970 (File No. 2-35965, Exhibit 4-2); Sixth Supplemental Indenture, dated as of October 1, 1973 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-3); Seventh Supplemental Indenture, dated as of February 15, 1977 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-4); and Eighth Supplemental Indenture, dated as of September 15, 1980 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-5). |
|-----|---|



---

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM 10-K**

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 1986      Commission File Number 2-35965

**NORTH SHORE GAS COMPANY**

(Exact name of registrant as specified in its charter)

**Illinois**

(State or other jurisdiction of  
incorporation or organization)

**36-1558720**

(IRS Employer  
Identification No.)

**122 South Michigan Avenue, Chicago, Illinois**

(Address of principal executive offices)

**60603**

(Zip Code)

**Registrant's telephone number, including area code:**  
**(312) 431-4000**

**Securities registered pursuant to Section 12(b) of the Act:   None**

**Securities registered pursuant to Section 12(g) of the Act:   None**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days.   Yes ☒   No ☐

State the aggregate market value of the voting stock held by non-affiliates of the registrant:

Redeemable Cumulative Preferred Stock, \$4,000,000 at November 30, 1986, based on the price at which the stock was sold.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, without par value, 3,625,887 shares outstanding at November 30, 1986.

Documents Incorporated by Reference  
None

---

# CONTENTS

<u>Item No.</u>		<u>Page No.</u>
	<u>Part I</u>	
1.	Business	3
2.	Properties	8 9
3.	Legal Proceedings	8 9
4.	Submission of Matters to a Vote of Security Holders	8 9
	<u>Part II</u>	
5.	Market for the Company's Common Stock and Related Stockholder Matters	<del>8</del> 10
6.	Selected Financial Data	<del>8</del> 10
7.	Management's Discussion and Analysis of Results of Operations and Financial Condition	<del>10</del> 11
8.	Financial Statements and Supplementary Data	<del>12</del> 13
9.	Disagreements on Accounting and Financial Disclosure	<del>12</del> 13
	<u>Part III</u>	
10.	Directors and Executive Officers of the Company	<del>29</del> 30
11.	Executive Compensation	<del>31</del> 32
12.	Security Ownership of Certain Beneficial Owners and Management	<del>31</del> 32
13.	Certain Relationships and Related Transactions	<del>32</del> 33
	<u>Part IV</u>	
14.	Exhibits, Financial Statement Schedules and Reports on Form 8-K	<del>33</del> 34
	Signatures	<del>41</del> 42
	Exhibit Index	<del>42</del> 43

North Shore Gas Company

ANNUAL REPORT ON FORM 10-K

FISCAL YEAR ENDED SEPTEMBER 30, 1986

PART I

ITEM 1. BUSINESS

GENERAL

North Shore Gas Company (Company) is an operating public utility engaged primarily in the purchase, storage, distribution and sale of natural gas at retail to approximately 103,000 residential, commercial and industrial customers within its service area of approximately 275 square miles, located in northeastern Illinois. It serves 56 communities and adjacent areas, including those situated along Lake Michigan from Winnetka, Illinois to the Illinois-Wisconsin state line. This area, with an estimated population of 354,000, contains residential concentrations and a diversity of industrial and commercial establishments, as well as some farm lands. The Company had 234 employees at September 30, 1986.

The Company holds certificates of public convenience and necessity issued by the Illinois Commerce Commission (Commission) for the conduct by the Company of its operations in the territory which it serves. It holds a license agreement from Lake County, Illinois, and, with minor exceptions, franchises from all of the incorporated cities and villages in its service territory. The franchises are of various terms and expiration dates, and are generally subject to various other conditions, restrictions or limitations not deemed materially burdensome.

At September 30, 1986, all of the common stock of the Company and of its affiliate, The Peoples Gas Light and Coke Company (Peoples Gas), was wholly-owned by Peoples Energy Corporation (Peoples Energy).

COMPETITION

Competition in varying degrees exists between natural gas and other fuels or forms of energy available to consumers in the Company's service area. Natural gas prices declined during the last year enabling gas to maintain a lower price than competing energies, except for certain fuel oils usable on a large volume basis by a small number of large-volume customers with dual-fuel capability. Overall, natural gas prices in the Company's service area compared very favorably on a national basis. The possibility of new or improved sources or uses of energy, limitations on future gas supply, changes in relative prices of competing fuels and energy, changes in environmental controls, increased use of transportation and other factors could, in the future, affect the Company's business. See "Federal Legislation and Regulation".

## ITEM 1. BUSINESS (Continued)

### SALES AND RATES

The Company sells natural gas having an average heating value of approximately 1,000 British thermal units (Btu's) per cubic foot.\* Sales are made and service rendered by the Company pursuant to rate schedules on file with the Commission containing various service classifications largely reflecting customers' different uses and size of consumption. Monthly adjustments to the Gas Charge under the Company's rate schedules provide for the pass-through of the increases or decreases in natural gas supplier rates, purchased storage service costs, transportation charges, liquefied petroleum gas costs and purchases of synthetic natural gas (SNG). In addition, under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or a current asset (with a contra entry to gas costs), and the fiscal-year balance is amortized over the 12-month period beginning the following January 1.

The Company has experienced load losses resulting from economic conditions and conservation efforts by customers. The basic marketing plan of the Company is to retain its strong position in the residential market while seeking expansion of the commercial and industrial markets.

### STATE LEGISLATION AND REGULATION

The Company is subject to the jurisdiction of and regulation by the Commission, which has general supervisory and regulatory powers over practically all phases of the public utility business in Illinois, including rates and charges, issuance of securities, services and facilities, systems of accounts, investments, safety standards, transactions with affiliated interests, as defined in the Illinois Public Utilities Act, and other matters.

In late fiscal 1984, the Commission granted the Company a rate increase of \$7.1 million on an annual basis. The Company was allowed a 12.47 per cent rate of return on its original cost rate base which reflects a 15.6 per cent cost of common equity. The new rates became effective in September, 1984.

Illinois legislation (Legislation) was enacted that requires the Commission to implement on a three-year trial basis regulations that, in general, prohibit a utility from discontinuing service to any low-income customer who is eligible for assistance in paying his heating bills under the Illinois Home Energy Assistance Program, provided such customer pays a specified portion of his income to the utility. Under this Legislation, a qualified low-income customer will not be required to pay a gas utility more than eight per cent of such customer's income during the winter heating season. The Company could experience a rise in uncollectible accounts in the future due to the Legislation and the Commission's regulations thereunder, but the Company cannot reasonably determine at this time the future impact of this Legislation.

---

\* All volumes of natural gas set forth in this report are stated on a 1,000 Btu (per cubic foot) billing basis.

ITEM 1. BUSINESS (Continued)

STATE LEGISLATION AND REGULATION (Continued)

The Commission has adopted the federal safety standards established under the Natural Gas Pipeline Safety Act of 1968 and is enforcing such standards with respect to the Company. The Company has a continuing program of inspection designed to keep all of its facilities in compliance with pipeline safety and pollution control requirements. The Company has made a complete inspection of all of its operational facilities and to the best of its knowledge is in substantial compliance with all pipeline safety and pollution control requirements.

FEDERAL LEGISLATION AND REGULATION

By Order entered on December 6, 1968 (Holding Company Act Release No. 16233), the Securities and Exchange Commission (SEC), pursuant to Section 3(a)(1) of the Public Utility Holding Company Act of 1935 (Act) exempted Peoples Energy and its subsidiary companies as such (including the Company) from the provisions of the Act other than Section 9(a)(2) thereof.

The Natural Gas Policy Act (NGPA), a major part of the National Energy Act enacted in 1978, instituted important changes in the laws affecting the natural gas industry. The NGPA (1) established ceiling prices at the wellhead for both interstate and previously unregulated intrastate gas, (2) deregulated the wellhead price of certain "high-cost" gas as of November 1, 1979, (3) deregulated the wellhead price of a major portion of the nation's gas supplies as of January 1, 1985, and (4) will deregulate the wellhead prices of gas in other categories in 1987. No material financial impact has resulted for the Company from NGPA deregulation provisions.

The NGPA also contains incremental pricing provisions which may result in increased rates to certain classes of industrial customers. These regulations are presently effective only for large industrial boilers. The Federal Energy Regulatory Commission (FERC) has, by rulemaking, exempted from incremental pricing all other industrial users which would otherwise be subject to these regulations under the terms of the statute. The Company has not experienced any adverse market effect due to the incremental pricing regulations.

Another part of the National Energy Act, entitled The Power Plant and Industrial Fuel Use Act, prohibits new electric power plants and new major fuel burning installations from using natural gas. Such end use limitations may result in lost market opportunities for the Company.

In late 1985, and early 1986, the FERC issued Order Nos. 436 and 436-A through E which, among other things, offer pipelines an option to transport gas on an "open-access" nondiscriminatory basis for all shippers under expedited regulatory procedures. Pipelines that elect this option are required, as a condition thereto, to allow firm sales customers to reduce their gas purchase demand volumes under firm sales contracts or convert such purchase demand to firm transportation service by up to 100 per cent over a five-year period following the pipeline's election.

ITEM 1. BUSINESS (Continued)

FEDERAL LEGISLATION AND REGULATION (Continued)

The 436 series of orders are on appeal to the Federal courts. However, a number of pipelines, including the sole supplier to the Company, have filed applications for open-access programs and have also elected to provide open-access transportation on an interim basis, pending resolution by FERC of specific operational, rate and other conditions of their proposed programs.

A number of the customers of the Company are substituting customer-owned gas for gas purchases from the Company, utilizing the availability of pipeline transportation as well as the Company's own transportation services. Under existing rates, the Company will experience no loss of distribution margin due to customer shifts from gas service to transportation service. The Company has utilized the increased availability of transportation to make purchases in the competitive spot market, thereby reducing the average cost of gas that must be recovered from customers.

Despite the access to spot market supplies afforded by open-access transportation, the Company is concerned because it is not known how the changing use of pipeline services under the new open-access rules will affect the security and reliability of long-term supplies from pipelines for distributors. (See, page , Note (a).)

Under one feature of Order No. 436, a pipeline may seek to provide transportation service directly to end-users. Such direct service by a pipeline to an end-user would bypass the local distributor's service and reduce its earnings. However, no such service has yet been proposed under the new Rule for any customers of the Company.

In December 1986, the FERC voted to deny rehearing of Order No. 451, which raised the ceiling prices permitted to be paid for all categories of "old" gas, still regulated under the NGPA, to that of the highest-priced old gas category. The Rule also established a "good faith negotiation" procedure by which producers of such gas may seek increased prices up to the new ceiling. A portion of contracted gas reserves of the pipeline suppliers for the Company is subject to this Rule. At this time, the Company cannot determine the ultimate impact on customers gas bills of Order No. 451, which is on appeal to the Federal courts. However, rates will not be affected during this winter.

GAS SUPPLY ADVANCES AND INVESTMENTS

During the natural gas shortage of the 1970's, the Company undertook several programs to augment its gas supply. From 1971, the Company, with Commission approval, made advance payments through a pipeline supplier and equity investments in gas and oil exploration and development ventures. At September 30, 1986, \$1.6 million in advances and equity investments remain outstanding. The Company is allowed by the Commission to include such advances and investments in the rate base and treat any profits or losses as utility transactions. See Note (11) of Notes to Consolidated Financial Statements for information on the Company's exploration subsidiary.

ITEM 1. BUSINESS (Continued)

CURRENT GAS SUPPLY

The following tabulation shows the expected peak-day availability of gas in thousand cubic feet (Mcf) during the 1986-87 heating season:

<u>Source</u>	<u>Peak-Day Availability (Mcf)</u>	<u>Year of Contract Expiration</u>
Flow Gas		
Natural.....	135,371	1990 (a)
Company (LP).....	<u>60,000</u>	
	<u>195,371</u>	
Storage Gas		
Natural.....	97,153 (b)	1987-1995 (a)
Peoples Gas (Manlove).....	<u>59,000 (c)</u>	1987
	<u>156,153</u>	
Total expected peak-day availability....	<u>351,524 (d)</u>	

- (a) Natural Gas Pipeline Company of America (Natural) may not terminate service at the expiration of service agreements without receiving prior authorization from the FERC.
- (b) The Company has storage service withdrawals available from Natural of (1) 53,029 Mcf per day subject to maximum seasonal withdrawal of 30 times the maximum daily withdrawal under a service agreement extending to 1990, (2) 6,657 Mcf per day under a service agreement extending to 1992, (3) 4,055 Mcf per day in the peak month, which is January, under a service agreement extending to 1991, (4) 3,412 Mcf per day under a service agreement extending to 1995, and (5) 30,000 Mcf per day under a service agreement expiring in 1987.
- (c) The Company has a gas storage agreement with Peoples Gas which provides a maximum withdrawal of 59,000 Mcf of storage service per day. The agreement also makes available "needle peaking" capacity at the discretion of Peoples Gas.
- (d) See discussion of Order No. 436 under Federal Legislation and Regulation.

ITEM 1. BUSINESS (Continued)

CURRENT GAS SUPPLY (Continued)

The Company's sources of gas supply (including gas transported for customers) in million cubic feet (MMcf) for the three fiscal years ended September 30, 1986, 1985 and 1984 are as follows:

	<u>1986</u>	<u>1985</u>	<u>1984</u>
Source:			
Natural (a)	31,625	31,802	33,630
Other Suppliers (a)	1,194	--	--
Peoples Gas - SNG (b)	944	841	738
Liquefied Petroleum Gas Produced	3	18	48
Customer Owned Gas - Received	17	--	--
Underground Storage - Net	(559)	(207)	(94)
Company Use, Franchise Requirements and Unaccounted for Gas	<u>(148)</u>	<u>(432)</u>	<u>(698)</u>
Total	<u>33,076</u>	<u>32,022</u>	<u>33,624</u>

- (a) The Company is now making spot purchases. Such purchases are made on a month-to-month basis where they produce a significant savings in gas costs. (See discussion of Order No. 436 under, Federal Legislation and Regulation.)
- (b) North Shore's service agreement with Peoples Gas which provided for the purchase of 10 per cent of the production of Peoples Gas' SNG plant, expired in fiscal 1986 and was not renewed.



## ITEM 2. PROPERTIES

All of the principal plants and properties of the Company have been maintained in the ordinary course of business and are believed to be in satisfactory operating condition. The following is a brief description of the principal plants and operating units of the Company.

The distribution system of the Company, as of September 30, 1986, consists of 1,695 miles of distribution mains and necessary pressure regulators, approximately 96,000 services (pipe connecting the mains with piping on the customers' premises) and approximately 106,000 meters installed on customers' premises. The Company has liquefied petroleum gasification and storage facilities. It also owns and has a substantial investment in office and service buildings, garages, repair shops and motor vehicles, together with the equipment, tools and fixtures necessary to conduct its business.

Most of the principal plants and properties of the Company, other than mains, services, meters, regulators and cushion gas in underground storage, are located on property owned in fee. Substantially all gas mains are installed in public streets, alleys and highways, or under property owned by others under grants of easements. Meters and house regulators in use and a portion of services are located on premises being served.

Substantially all of the physical properties now owned or hereafter acquired by the Company are subject to (a) the direct, first mortgage lien of the Company's Mortgage to the Continental Illinois National Bank and Trust Company of Chicago, Trustee, to secure the principal amount of the Company's First Mortgage Bonds outstanding at September 30, 1986 and (b) in certain cases, other exceptions and defects which do not interfere with the use of the property.

## ITEM 3. LEGAL PROCEEDINGS

There are no material legal proceedings pending to which the Company is a party.

## ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

PART II

ITEM 5. MARKET FOR THE COMPANY'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The Company is a wholly-owned subsidiary of Peoples Energy.

ITEM 6. SELECTED FINANCIAL DATA

For fiscal years ended September 30,	1986	1985	1984	1983	1982
<u>OPERATING RESULTS (thousands)</u>					
Operating Revenues:					
Residential	\$ 96,265	\$ 99,472	\$ 98,818	\$ 85,984	\$ 90,465
Commercial	38,133	40,837	40,319	35,532	36,325
Industrial	30,409	34,052	32,765	29,845	27,994
Transportation of customer-owned gas	7	--	--	--	--
Other	944	966	1,199	1,374	1,708
Total Operating Revenues	<u>165,758</u>	<u>175,327</u>	<u>173,101</u>	<u>152,735</u>	<u>156,492</u>
Less - Gas costs	108,893	118,789	122,314	108,049	109,629
- Revenue taxes	11,094	12,026	11,598	10,541	11,049
Net Operating Revenues	<u>\$ 45,771</u>	<u>\$ 44,512</u>	<u>\$ 39,189</u>	<u>\$ 34,145</u>	<u>\$ 35,814</u>
Net Income Applicable to Common Stock	\$ 8,900	\$ 8,782	\$ 6,847	\$ 4,549	\$ 5,719
<u>GAS SOLD AND TRANSPORTED (million cubic feet)</u>					
Residential	18,161	17,209	18,323	16,378	18,777
Commercial	8,090	7,946	8,377	7,563	8,361
Industrial	6,806	6,867	6,924	6,369	6,374
Transportation of customer-owned gas	19	--	--	--	--
Total	<u>33,076</u>	<u>32,022</u>	<u>33,624</u>	<u>30,310</u>	<u>33,512</u>
<u>NUMBER OF CUSTOMERS (average)</u>					
Residential	96,281	94,393	93,126	92,256	91,769
Commercial	5,962	5,769	5,595	5,487	5,356
Industrial	717	700	695	655	631
Transportation	1	--	--	--	--
Total	<u>102,961</u>	<u>100,862</u>	<u>99,416</u>	<u>98,398</u>	<u>97,756</u>
<u>DEGREE DAYS</u>					
Per cent of normal (6,455)	105	103	111	97	112
<u>ASSETS (thousands)</u>					
Property, plant and equipment	\$138,601	\$128,767	\$121,629	\$116,888	\$110,993
Less-Accumulated depreciation	45,299	41,803	38,477	35,873	32,547
Net Property, Plant and Equipment	<u>\$ 93,302</u>	<u>\$ 86,964</u>	<u>\$ 83,152</u>	<u>\$ 81,015</u>	<u>\$ 78,446</u>
Capital expenditures - construction	\$ 10,810	\$ 8,072	\$ 6,186	\$ 6,480	\$ 4,869
Total Assets	<u>\$123,957</u>	<u>\$130,756</u>	<u>\$122,780</u>	<u>\$131,546</u>	<u>\$126,041</u>
<u>CAPITALIZATION AT YEAR END (thousands)</u>					
Common equity	\$ 44,295	\$ 41,197	\$ 39,086	\$ 37,824	\$ 36,937
Preferred stock	3,000	4,000	5,000	6,000	7,000
Long-term debt	27,625	33,082	38,494	39,936	41,204
Total	<u>\$ 74,920</u>	<u>\$ 78,279</u>	<u>\$ 82,580</u>	<u>\$ 83,760</u>	<u>\$ 85,141</u>
<u>CAPITALIZATION RATIOS AT YEAR END (per cent)</u>					
Common equity	59	53	47	45	43
Preferred stock	4	5	6	7	8
Long-term debt	37	42	47	48	49
Total	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>

The Company is a wholly-owned subsidiary of Peoples Energy; therefore, cash dividends declared per share and earnings per share are omitted.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION

Results of Operations

Net income applicable to common stock increased by \$118,000 in 1986 mainly due to colder weather than the prior year. The increase in 1985 was mainly due to a rate increase which became effective in late 1984. This increase was offset, in part, by a reduction in gas sales due to warmer weather than in 1984.

Weather variations affect the volumes of gas sold for heating and, therefore, can have a significant impact on net income. The effect on net income of the major operating cost - that of gas purchased or produced - is mitigated because such costs are recovered from customers through the gas cost recovery provision in the Company's rate schedules. A summary of significant variations in income is presented below, with explanations following:

(Thousands of dollars)	Fiscal 1986 Over 1985		Fiscal 1985 Over 1984	
	Amount	%	Amount	%
Net operating revenues*	\$1,259	2.8	\$5,323	13.6
Operation and maintenance expenses	1,434	8.3	(436)	(2.4)
Income taxes	(582)	(6.2)	2,383	34.1
Other income	(205)	(12.6)	(515)	(24.0)
Net Income Applicable to Common Stock	118	1.3	1,935	28.3

\* Operating revenues net of gas costs and revenue taxes.

( ) Denotes red figure.

The increase in 1986 net operating revenues results mainly from colder weather than in the prior year. The increase in 1985 results mainly from a rate increase which became effective late in 1984, offset in part, by weather that was warmer than the previous year.

The increase in operation and maintenance expenses for 1986, primarily is due to increased costs of materials and services, higher labor costs reflecting higher wages and increased collection-related expenses.

The change in income taxes in both periods mainly reflects changes in pre-tax income.

The decrease in other income in both periods is mainly due to lower interest rates.

Liquidity and Capital Resources

The Company has access to outside capital markets and to internal sources of funds that together should provide sufficient resources to meet capital requirements. The Company does not anticipate any changes that materially would alter its current liquidity position.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF RESULTS OF OPERATIONS AND FINANCIAL CONDITION (Continued)

Liquidity and Capital Resources (Continued)

Due to the seasonal nature of gas sales, a major portion of cash collections occurs between November and April. Because of timing differences in the receipt and disbursement of cash, and the level of construction requirements, the Company may borrow on a short-term basis. Short-term borrowings are either repaid with cash from operations or refinanced on a permanent basis with debt and/or equity, depending on money-market conditions and capital structure considerations.

On September 15, 1986, North Shore redeemed, at par, \$3.0 million of its First Mortgage 12% Bonds, Series H, due September 15, 1995. The redemption was effected by a scheduled sinking fund payment of \$1.5 million plus an optional sinking fund payment of \$1.5 million.

Additional bonds are issuable, upon Commission approval, subject to limitations by certain restrictive provisions of the open-end mortgages and supplements thereto. Short-term cash needs are met through borrowing arrangements with banks and/or the issuance of commercial paper. See Note (9) of Notes to Consolidated Financial Statements.

Capital expenditures for additions, replacements and improvements of the utility plant were \$10.8 million in 1986, \$8.1 million in 1985 and \$6.2 million in 1984. Total capital expenditures for fiscal 1987 are estimated to be \$14.4 million.

The impact of the Tax Reform Act of 1986 is not expected to have a material effect on the Company's cash flow.

See Note (14) of Notes to Consolidated Financial Statements for an estimate of the impact of inflation on the Company.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

	<u>Page</u>
Report of Independent Public Accountants	13
Statements of Consolidated Income for the fiscal years ended September 30, 1986, 1985 and 1984	14
Statements of Consolidated Retained Earnings for fiscal years ended September 30, 1986, 1985 and 1984	14
Consolidated Balance Sheets as of September 30, 1986 and 1985	15
Consolidated Capitalization Statements as of September 30, 1986 and 1985	16
Consolidated Statements of Changes in Financial Position for the fiscal years ended September 30, 1986, 1985 and 1984	17
Notes to the Consolidated Financial Statements	18
Selected Quarterly Financial Data	28

ITEM 9. DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To North Shore Gas Company:

We have examined the consolidated balance sheets and capitalization statements of North Shore Gas Company (an Illinois corporation, hereinafter referred to as the Company and a wholly-owned subsidiary of Peoples Energy Corporation) and subsidiary companies as of September 30, 1986 and 1985, and the related statements of consolidated income, retained earnings and changes in financial position for each of the three fiscal years in the period ended September 30, 1986. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of the Company and subsidiary companies as of September 30, 1986 and 1985, and the results of their operations and changes in financial position for each of the three fiscal years in the period ended September 30, 1986, in conformity with generally accepted accounting principles applied on a consistent basis.

Our examinations were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The financial statement schedules listed in Item 14(a)2 are presented for purposes of complying with the Securities and Exchange Commission's rules and regulations under the Securities Exchange Act of 1934 and are not part of the basic financial statements. These schedules have been subjected to the auditing procedures applied in the examinations of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN & CO.

Chicago, Illinois  
November 5, 1986

North Shore Gas Company

STATEMENTS OF CONSOLIDATED INCOME  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1986	1985	1984
OPERATING REVENUES:			
Gas sales	\$164,807	\$174,361	\$171,902
Other	951	966	1,199
Total Operating Revenues	<u>165,758</u>	<u>175,327</u>	<u>173,101</u>
OPERATING EXPENSES:			
Gas costs	108,893	118,789	122,314
Operation	16,345	15,258	15,698
Maintenance	2,453	2,106	2,102
Depreciation	4,343	4,106	3,891
Taxes - Income	8,789	9,371	6,988
- State and local revenue	11,094	12,026	11,598
- Other	1,362	1,339	1,325
Total Operating Expenses	<u>153,279</u>	<u>162,995</u>	<u>163,916</u>
OPERATING INCOME	12,479	12,332	9,185
OTHER INCOME:			
Interest income	1,234	1,491	2,051
Miscellaneous	190	138	93
Total Other Income	<u>1,424</u>	<u>1,629</u>	<u>2,144</u>
GROSS INCOME	13,903	13,961	11,329
INCOME DEDUCTIONS:			
Interest on long-term debt	3,521	3,693	3,795
Other interest	1,080	1,005	124
Amortization of debt discount and expense	23	24	24
Miscellaneous	1	--	4
Total Income Deductions	<u>4,625</u>	<u>4,722</u>	<u>3,947</u>
NET INCOME	9,278	9,239	7,382
Preferred stock dividends	<u>378</u>	<u>457</u>	<u>535</u>
NET INCOME APPLICABLE TO COMMON STOCK	<u>\$ 8,900</u>	<u>\$ 8,782</u>	<u>\$ 6,847</u>

STATEMENTS OF CONSOLIDATED RETAINED EARNINGS  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	1986	1985	1984
BALANCE AT BEGINNING OF YEAR	\$ 16,440	\$ 14,329	\$ 13,067
Add - Net income	9,278	9,239	7,382
Deduct - Dividends on common stock	5,802	6,671	5,585
- Dividends on preferred stock	<u>378</u>	<u>457</u>	<u>535</u>
BALANCE AT END OF YEAR	<u>\$ 19,538</u>	<u>\$ 16,440</u>	<u>\$ 14,329</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company  
CONSOLIDATED BALANCE SHEETS  
(Thousands of Dollars)

	As of September 30,	
	1986	1985
<b>PROPERTIES AND OTHER ASSETS</b>		
<b>CAPITAL INVESTMENTS:</b>		
Property, plant and equipment, at original cost	\$138,601	\$128,767
Less - Accumulated depreciation	45,299	41,803
	<u>93,302</u>	<u>86,964</u>
Gas supply advances and investments	1,564	1,850
<b>TOTAL CAPITAL INVESTMENTS</b>	<u>94,866</u>	<u>88,814</u>
<b>CURRENT ASSETS:</b>		
Cash	769	1,592
Temporary cash investments, at cost that approximates market value	--	12,000
Receivables -		
Customers, net of allowance for uncollectible accounts of \$634 and \$714, respectively	5,338	5,455
Other	222	115
Materials and supplies, at average cost	1,396	1,323
Gas in storage, at last-in, first-out cost	20,136	18,956
Gas costs recoverable through rate adjustments	5	1,560
Prepayments	443	209
<b>TOTAL CURRENT ASSETS</b>	<u>28,309</u>	<u>41,210</u>
<b>DEFERRED CHARGES</b>	<u>782</u>	<u>732</u>
<b>TOTAL PROPERTIES AND OTHER ASSETS</b>	<u>\$123,957</u>	<u>\$130,756</u>
<b>CAPITALIZATION AND LIABILITIES</b>		
<b>CAPITALIZATION</b> (see accompanying statement)	\$ 74,920	\$ 78,279
<b>CURRENT LIABILITIES:</b>		
Accounts payable	7,503	9,519
Dividends payable on preferred stock	10	20
Customer deposits	4,819	5,173
Sinking fund payments and maturities		
Long-term debt	3,707	4,912
Redeemable cumulative preferred stock	1,000	1,000
Accrued taxes	1,092	989
Gas sales revenue refundable	9,828	10,031
Accrued interest	280	367
<b>TOTAL CURRENT LIABILITIES</b>	<u>28,239</u>	<u>32,011</u>
<b>RESERVES AND DEFERRED CREDITS:</b>		
Deferred income taxes - primarily accelerated depreciation	15,030	14,500
Investment tax credits being amortized over the average lives of related property	5,140	5,198
Other	628	768
<b>TOTAL RESERVES AND DEFERRED CREDITS</b>	<u>20,798</u>	<u>20,466</u>
<b>TOTAL CAPITALIZATION AND LIABILITIES</b>	<u>\$123,957</u>	<u>\$130,756</u>

The accompanying notes are an integral part of these statements.



North Shore Gas Company

CONSOLIDATED CAPITALIZATION STATEMENTS  
(Thousands of Dollars)

	As of September 30,	
	<u>1986</u>	<u>1985</u>
COMMON STOCKHOLDER'S EQUITY:		
Common stock, without par value		
Authorized 5,000,000 shares,		
Outstanding 3,625,887 shares	\$ 24,757	\$ 24,757
Retained earnings (see accompanying statement)	<u>19,538</u>	<u>16,440</u>
TOTAL COMMON STOCKHOLDER'S EQUITY	44,295	41,197
REDEEMABLE CUMULATIVE PREFERRED STOCK:		
Exclusive of sinking fund payments, due within one year		
Authorized 200,000 and 210,000 shares, respectively,		
par value \$100		
7-7/8% Series, 0 and 10,000 shares outstanding,		
respectively	--	1,000
9% Series, 30,000 shares outstanding	<u>3,000</u>	<u>3,000</u>
TOTAL REDEEMABLE CUMULATIVE PREFERRED STOCK	3,000	4,000
LONG-TERM DEBT:		
Exclusive of sinking fund payments and maturities,		
due within one year		
First Mortgage Bonds -		
5% Series C, due December 1, 1986	--	1,607
9-1/2% Series E, due February 1, 1995	6,625	6,625
8-3/8% Series F, due October 1, 1998	7,500	7,750
8-3/8% Series G, due February 15, 1992	3,000	3,600
12% Series H, due September 15, 1995	<u>10,500</u>	<u>13,500</u>
TOTAL LONG-TERM DEBT	<u>27,625</u>	<u>33,082</u>
TOTAL CAPITALIZATION	<u>\$ 74,920</u>	<u>\$ 78,279</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	<u>1986</u>	<u>1985</u>	<u>1984</u>
FUNDS PROVIDED:			
Net income	\$ 9,278	\$ 9,239	\$ 7,382
Add - Principal items not requiring current outlay of funds			
Depreciation	4,343	4,106	3,891
Deferred income taxes - primarily accelerated depreciation	1,264	1,353	1,122
Deferred investment tax credits - net	<u>13</u>	<u>430</u>	<u>345</u>
TOTAL FUNDS PROVIDED FROM OPERATIONS	14,898	15,128	12,740
Other	<u>--</u>	<u>591</u>	<u>789</u>
TOTAL FUNDS PROVIDED	<u>\$ 14,898</u>	<u>\$15,719</u>	<u>\$13,529</u>
FUNDS APPLIED:			
Capital expenditures - construction	\$ 10,810	\$ 8,072	\$ 6,186
Reduction of:			
Long-term debt	6,662	1,444	1,443
Preferred stock	1,000	1,000	1,000
Dividends on common stock	5,802	6,671	5,585
Dividends on preferred stock	378	457	535
Decrease in working capital	(10,333)	(1,925)	(1,220)
Other	<u>579</u>	<u>--</u>	<u>--</u>
TOTAL FUNDS APPLIED	<u>\$ 14,898</u>	<u>\$15,719</u>	<u>\$13,529</u>
INCREASE (DECREASE) IN WORKING CAPITAL, EXCLUSIVE OF CURRENT MATURITIES OF LONG-TERM DEBT AND SINKING FUND PAYMENTS, BY COMPONENT:			
Cash and temporary cash investments	\$(12,823)	\$ 3,847	\$(9,802)
Receivables and payables - net	2,016	850	3,682
Gas in storage	1,180	116	(146)
Rate adjustments refundable or recoverable	(1,353)	(3,947)	2,116
Accrued taxes	(103)	(1,990)	2,949
Customer deposits	355	(322)	(129)
Materials and supplies	73	(576)	136
Other	<u>322</u>	<u>97</u>	<u>(26)</u>
DECREASE IN WORKING CAPITAL	<u>\$(10,333)</u>	<u>\$(1,925)</u>	<u>\$(1,220)</u>

The accompanying notes are an integral part of these statements.

( ) Denotes red figure.

STATEMENT OF MANAGEMENT

These financial statements were prepared by management, which is responsible for their integrity and objectivity. The statements are in conformity with generally accepted accounting principles and, as such, reflect judgments made by management.

Based upon the Company's accounting and internal control systems, along with ongoing internal audit programs, management believes that the accounting records are reliable for the purpose of preparing financial statements, and assets are appropriately safeguarded against loss from unauthorized use.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) SIGNIFICANT ACCOUNTING POLICIES

a. Principles of Consolidation

All subsidiaries of the Company are included in the consolidated financial statements. All significant intercompany transactions have been eliminated in consolidation. Certain items previously reported for years prior to 1986 have been reclassified to conform with the current-year presentation.

b. Property, Plant and Equipment

Property, plant and equipment is stated at original cost and includes appropriate amounts of payroll taxes, employee-benefit costs, administrative costs, and an allowance for funds used during construction.

c. Allowance for Funds Used During Construction

The assumed cost of all funds used to finance substantial and lengthy construction is capitalized as a cost element of Utility Plant, with an offsetting credit to Other Income. Under established regulatory practices, the Company is permitted to include in its rates a fair return on, and the recovery of, these capitalized costs by including them in rate base and in the provision for depreciation.

There was no allowance for funds used during construction in fiscal years 1986, 1985 and 1984.

d. Maintenance and Depreciation

It is the practice of the Company to charge to maintenance the cost of repairs, renewals, and improvements amounting to less than retirement units of property. When depreciable property is retired, its original cost is charged to the accumulated provision for depreciation.

The provision for depreciation substantially reflects the systematic amortization of the original cost of depreciable property over the estimated useful lives on the straight-line method.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

d. Maintenance and Depreciation (Continued)

Additionally, actual dismantling cost, net of salvage, is included in the provision for depreciation in the month incurred. The amounts provided are designed to cover not only losses due to wear and tear that are not restored by maintenance, but also losses due to obsolescence and inadequacy.

The provision for depreciation, expressed as an annual percentage of original cost of depreciable property, approximated 3.7%, 3.7% and 3.6% for fiscal years 1986, 1985 and 1984, respectively.

e. Recovery of Gas Costs

Under the tariffs of the Company, the difference for any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is refunded or recovered over a 12-month billing cycle beginning the following January 1. Consistent with these tariff provisions, such difference for any month is recorded either as a current liability or a current asset (with a contra entry to gas costs), and the fiscal-year balance is amortized over the 12-month period beginning the following January 1.

f. Gas in Storage

Storage injections are priced at the fiscal-year average of demand and commodity costs of natural gas purchased and synthetic natural gas (SNG) purchased. Withdrawals from storage are priced on the last-in, first-out (LIFO) method. The estimated current replacement cost of gas in inventory exceeded the LIFO cost by approximately \$30 million and \$37 million at September 30, 1986 and 1985, respectively.

g. Taxes

For federal and Illinois income-tax purposes, for periods prior to January 1, 1981, the Company adopted liberalized methods of computing depreciation on property additions after December 31, 1953, and the Asset Depreciation Range (ADR) system on property additions after December 31, 1970. For periods after December 31, 1980, the Company is utilizing the Accelerated Cost Recovery System (ACRS).

Deferred income taxes for the difference between tax depreciation computed on these methods and straight-line depreciation are charged to income and credited to accumulated deferred income taxes. This account is charged when liberalized, ADR, or ACRS tax depreciation becomes less than straight-line depreciation.

The investment tax credits have been deferred and are being amortized through credits to income over the book lives of related property. The Tax Reform Act of 1986, signed into law on October 22, 1986, repeals the investment tax credit for property placed in service after December 31, 1985, subject to certain transition rules.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

At September 30, 1986, the cumulative net amount of timing differences for which deferred income taxes have been over provided is approximately \$1 million.

The preceding deferred-tax and tax-credit accounting conforms with regulations of the Commission.

(2) PENSION PLANS AND POST-RETIREMENT BENEFITS

The Company participates in two defined benefit pension plans covering substantially all employees. Total pension expenses for fiscal years 1986, 1985, and 1984 were \$1.3 million, \$1.2 million, and \$1.1 million, respectively.

The Company has made annual contributions to the plans equal to the amounts accrued for pension expenses, including amortization of past service costs over periods varying from 15 to 25 years. Accumulated plan benefit information, as furnished by consulting actuaries, and plan net assets for the Company's pension plans are:

	As of October 1,	
	1985	1984
	(Millions)	
Actuarial present value of accumulated plan benefits:		
Vested	\$16.7	\$14.4
Nonvested	1.5	1.4
	<u>\$18.2</u>	<u>\$15.8</u>
Net assets available for benefits	<u>\$20.8</u>	<u>\$17.7</u>

The assumed rate of return used in determining the actuarial present value of accumulated plan benefits was 6.5 per cent for both 1985 and 1984.

In addition to providing pension benefits, the Company provides certain health-care and life-insurance benefits for retired employees. Substantially all employees may become eligible for such benefit coverage if they reach retirement age while working for the Company. The costs of providing these benefits, which are unfunded, are expensed on the Company's books when paid and amounted to \$154,000 for fiscal 1986.

In December 1985, the FASB issued a new statement entitled "Employers' Accounting for Pensions," which supersedes previous pension accounting standards and will be effective for fiscal years beginning after December 15, 1986. This statement prescribes a standardized method for measuring net periodic pension costs, expanded footnote disclosures, and, in some cases, recognition of a pension liability. The Company plans to adopt this statement in fiscal 1987.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(3) COVENANTS REGARDING RETAINED EARNINGS

The Company's Indenture relating to the First Mortgage Bonds and the Stock Purchase Agreements relating to the Cumulative Preferred Stock contain provisions and covenants restricting the payment of cash dividends and the purchase or redemption of capital stock. At September 30, 1986, such restrictions amounted to \$5.3 million out of total retained earnings of \$19.5 million.

(4) TAX MATTERS

Provision for Income Taxes For fiscal years ended September 30,	<u>1986</u>	<u>1985</u>	<u>1984</u>
	(000's)		
Current:			
Federal	\$ 6,497	\$ 6,554	\$ 4,658
State	<u>1,015</u>	<u>1,034</u>	<u>863</u>
Total current income taxes	<u>7,512</u>	<u>7,588</u>	<u>5,521</u>
Deferred, net - Primarily accelerated depreciation			
Federal	1,102	1,181	980
State	<u>162</u>	<u>172</u>	<u>142</u>
Total deferred income taxes - Primarily accelerated depreciation	<u>1,264</u>	<u>1,353</u>	<u>1,122</u>
Investment tax credits - net:			
Federal	(21)	395	325
State	<u>34</u>	<u>35</u>	<u>20</u>
Total investment tax credits - net	<u>13</u>	<u>430</u>	<u>345</u>
Total provision for income taxes	<u>\$ 8,789</u>	<u>\$ 9,371</u>	<u>\$ 6,988</u>
Included in operating expenses as taxes - income	<u>\$ 8,789</u>	<u>\$ 9,371</u>	<u>\$ 6,988</u>

( ) Denotes red figure.

Total investment tax credits excludes \$.4 million generated after the effective date of the repeal under the Tax Reform Act of 1986. This amount has been included in current federal income tax expense.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(4) TAX MATTERS (Continued)

The following is a reconciliation between the computed federal income tax expense (statutory rate of 46 per cent times pre-tax income) and the total provision for federal income tax expenses:

For fiscal years ended September 30,	1986		1985		1984	
	Amount (000's)	Per Cent of Pre-tax Income	Amount (000's)	Per Cent of Pre-tax Income	Amount (000's)	Per Cent of Pre-tax Income
Computed federal income tax expense	\$7,754	46.0	\$7,990	46.0	\$6,139	46.0
Amortization of investment tax credit	(249)	(1.5)	(241)	(1.4)	(235)	(1.8)
Book depreciation over depreciation used in tax provision	75	0.5	78	0.5	60	0.5
Other	(2)	--	303	1.7	(1)	--
Total provision for federal income taxes	<u>\$7,578</u>	<u>45.0</u>	<u>\$8,130</u>	<u>46.8</u>	<u>\$5,963</u>	<u>44.7</u>

( ) Denotes red figure.

Tax returns for 1980 through 1982 have been audited by the Internal Revenue Service and a tax deficiency of approximately \$508,000 has been proposed. Issues are being contested, and the potential impact on net income is not believed to be material since the issues consist of income tax provision timing differences.

Tax returns for 1983 and 1984 are currently under audit by the Internal Revenue Service.

(5) DEFERRED CHARGES

	As of September 30,	
	1986	1985
	(000's)	
Interest on gas sales revenue refundable	\$463	\$419
Debt expense being amortized over the lives of outstanding issues	174	198
Energy Conservation Plan expenses	110	78
Other	35	37
	<u>\$782</u>	<u>\$732</u>

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(6) COMMON STOCK

No common stock was issued during the fiscal years 1984 through 1986.

(7) REDEEMABLE CUMULATIVE PREFERRED STOCK

	<u>7.875% Series</u>	<u>9.0% Series</u>
Year of issue	1977	1980
Shares outstanding	10,000(a)	30,000
Involuntary liquidation preference (000's)	\$ 1,000	\$ 3,000
Annual dividends per share	\$ 7.875	\$ 9.00
Redemption options:		
Currently effective redemption price per share	\$100.00	(b)
Redemption price per share decreases annually to issue price by (year)	--	(b)
Redemption through certain refunding operations not permitted prior to (year)	--	1990

(a) Shares outstanding were reduced by 10,000 during fiscal 1986 to meet sinking fund requirements.

(b) Not currently redeemable at the option of the Company.

(8) SINKING FUND REQUIREMENTS

Sinking fund requirements of preferred stock outstanding at September 30, 1986, are \$1.0 million for fiscal year 1987. There are no sinking fund requirements for fiscal years 1988 through 1990 and \$3.0 million for fiscal year 1991.

Sinking fund requirements and maturities of long-term debt outstanding at September 30, 1986, for fiscal years 1987 through 1991 are \$3.7 million for 1987 and \$2.4 million for 1988 and \$2.6 million each year for 1989 through 1991.

(9) SHORT-TERM BORROWING AND COMPENSATING BALANCES

Short-term cash needs of the Company are met through bank loans and/or the issuance of commercial paper. The outstanding total amount of these borrowings cannot at any time exceed total bank credit then in effect.



North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(9) SHORT-TERM BORROWING AND COMPENSATING BALANCES (Continued)

During fiscal 1986, Peoples Gas maintained \$100 million in bank credit through an irrevocable revolving credit agreement. This amount was reduced to \$63 million for fiscal 1987 and 1988, as projected short-term credit requirements used to support the long-term status of certain Adjustable-Rate Mortgage Bonds of Peoples Gas have been reduced. The Company may borrow up to \$15 million.

Payment for the revolving credit agreement with the banks is through compensating balances and/or fees. There were no legal restrictions on withdrawal of compensating balances.

(10) ASSETS SUBJECT TO LIEN

The Indenture of Mortgage, dated April 1, 1955, as supplemented, securing the First Mortgage Bonds issued by the Company, constitutes a direct, first-mortgage lien on substantially all property owned by the Company.

(11) EXPLORATION SUBSIDIARY

North Shore Exploration Company, a wholly-owned subsidiary of the Company, was formed in 1973 to engage, directly or indirectly, in lease-acquisition and exploration and development programs. The exploration unit has made investments totaling \$4.1 million and through September 30, 1986, has amortized \$3.4 million. The Company is allowed by the Commission to include such investments in its rate base and treat any profits or losses as utility transactions.

(12) TEMPORARY CASH INVESTMENTS

Temporary cash investments at September 30, 1985, consisted of Eurodollar Deposits maturing October 1, 1985.

(13) LEGAL PROCEEDINGS

There are no material legal proceedings pending to which the Company is a party.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(14) EFFECT OF CHANGING PRICES (Unaudited)

Consolidated financial statements in this report reflect the historical cost of Company assets. The following two tables were prepared in accordance with the Financial Accounting Standards Board (FASB) requirements relating to changing price information. The tables provide an estimate of the impact of inflation on the Company by presenting selected information on the basis of conventional historical cost and current cost. They should be viewed as estimates of the approximate effect of inflation, rather than a precise measure.

Current cost information reflects specific price changes from the date of acquisition of the asset to the present. The Handy-Whitman Index of Public Utility Construction Costs was used to develop specific prices.

Under established regulatory practices, utilities generally are limited to recovery of historical cost of their properties in rates charged to customers. When replacement of productive capacity is made by a utility, resulting in a higher historical cost, that utility can file for recovery of the increased depreciation expense and a return on the higher cost of replacement property. The amount by which the operating results are affected is dependent, in part, upon the timeliness and extent of such rate increases and cannot be projected.

During periods of inflation, amounts recovered from customers will have less purchasing power than historical dollars invested. As a result, excess cost of the utility plant - stated in terms of current cost over historical cost - is reflected as an adjustment to net recoverable cost. Part of the loss in purchasing power from amounts invested in utility assets is offset by the use of long-term debt and other fixed-return securities to finance a significant portion of these assets. The securities will be repaid with dollars having less value than those received when the securities were issued.

Depreciation expense was developed by applying historical depreciation rates to various property accounts, after the accounts were adjusted for specific price changes. Storage gas inventories and gas costs were not repriced because purchased gas costs are recovered dollar-for-dollar through the gas-cost recovery process. In accordance with FASB guidelines, income taxes have not been adjusted.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(14) EFFECT OF CHANGING PRICES (Unaudited) (Continued)

Income Adjusted for the Effect of Changing Prices:

	<u>Current Cost (Millions)</u>
Net income applicable to common stock as reported	<u>\$ 9</u>
Impact on net income due to additional depreciation and adjustment to net recoverable costs (a)	3
Reduction in economic obligation to repay net amounts owed	1
Specific price changes in excess of general price level changes	<u>(4)</u>
Net erosion of reported net income	<u>--</u>
Net income adjusted for the effect of changing prices (b)	<u>\$ 9</u>

( ) Denotes red figure.

(a) At September 30, 1986, the current cost of property, plant and equipment, net of accumulated depreciation, in nominal dollars, was \$216 million.

(b) Reported net income adjusted only for the additional depreciation and adjustment to net recoverable cost would be \$12 million.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(14) EFFECT OF CHANGING PRICES (Unaudited) (Continued)

Five-Year Comparison of Selected Supplementary Financial Data Adjusted for Effects of Changing Prices in Average 1986 Dollars:

	For fiscal years ended September 30,				
	<u>1986</u>	<u>1985</u>	<u>1984</u>	<u>1983</u>	<u>1982</u>
	(Millions)				
Operating revenues - As reported	\$ 166	\$ 175	\$ 173	\$ 153	\$ 157
- In average 1986 dollars	\$ 166	\$ 179	\$ 184	\$ 169	\$ 180

Current Cost Information:

Depreciation expense	\$ 10	\$ 10	\$ 10	\$ 9	\$ 10
Specific price changes in excess of general price-level changes	\$ (4)	\$ 1	\$ 3	\$ (1)	\$ 3
Net income adjusted for all effects of changing prices	\$ 9	\$ 8	\$ 6	\$ 4	\$ 5
Net assets at year-end	\$ 44	\$ 42	\$ 40	\$ 41	\$ 41

General Information:

Reduction in economic obligation to repay net amounts owed	\$ 1	\$ 1	\$ 2	\$ 1	\$ 2
Average consumer price index	327.3	319.4	308.1	296.0	286.0
Year-end consumer price index	330.2	324.5	314.5	301.8	293.3

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(15) SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	<u>Operating Revenues</u>	<u>Operating Income</u> (000's)	<u>Net Income Applicable to Common Stock</u>
First Quarter			
1986	\$ 45,575	\$ 3,738	\$ 2,667
1985	47,746	3,709	2,575
Second Quarter			
1986	73,719	7,259	6,295
1985	79,818	7,404	6,375
Third Quarter			
1986	30,101	1,580	968
1985	31,178	1,538	884
Fourth Quarter			
1986	16,363	(98)	(1,030)
1985	16,585	(319)	(1,052)
Fiscal Year			
1986	165,758	12,479	8,900
1985	175,327	12,332	8,782

---

( ) Denotes red figure.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY

IDENTIFICATION OF DIRECTORS

<u>Name, Principal Occupation and Other Directorships</u>	<u>Age at 11-30-86</u>	<u>Company Directorship Since</u>
Louis C. Baldacci, Jr. President and Chief Operating Officer of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	61	1976
J. Bruce Hasch Executive Vice President of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas	48	1986
James Hinchliff Vice President and General Counsel of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas.	46	1985
Donald G. Holm Vice President, Secretary and Treasurer of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas.	59	1982
Masao Igasaki, Jr. Vice President of the Company and Peoples Gas; Vice President and Controller of Peoples Energy; Director of Peoples Gas.	61	1982
Richard E. Terry Executive Vice President of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	49	1982
Eugene A. Tracy Chairman of the Board and Chief Executive Officer of the Company, Peoples Energy and Peoples Gas; Director of LaSalle National Bank.	58	1978

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY (Continued)

IDENTIFICATION OF EXECUTIVE OFFICERS

	<u>Position at November 30, 1986</u>	<u>Age at 11-30-86</u>	<u>Position Held Since</u>
Louis C. Baldacci, Jr.	President and Chief Operating Officer	61	1985
Patrick J. Doyle	Vice President	49	1985
J. Bruce Hasch	Executive Vice President	48	1985
James Hinchliff	Vice President and General Counsel	46	1984
Donald G. Holm	Vice President, Secretary and Treasurer	59	1981
Masao Igasaki, Jr.	Vice President	61	1977
John A. Lawrisuk	Vice President	58	1981
Ruel F. Lehman, Jr.	Vice President	63	1975
Michael S. Reeves	Vice President	51	1977
Richard E. Terry	Executive Vice President	49	1984
Eugene A. Tracy	Chairman of the Board and Chief Executive Officer	58	1981

Directors and executive officers of the Company were elected to serve for a term of one year or until their successors are duly elected and qualified.

There are no family relationships between directors and executive officers of the Company.

All of the directors and executive officers of the Company have been continuously employed by the Company and/or its affiliates in various capacities for at least 10 years.

## ITEM 11. EXECUTIVE COMPENSATION

The executive officers of the Company serve both the Company and its affiliate Peoples Gas. Remuneration is paid by Peoples Gas with appropriate amounts billed to the Company for the time such officers serve North Shore. The Company was billed \$342,503 for the services of these officers during fiscal 1986, including approximately \$63,000 for the services of Mr. Tracy. No other executive officer's cash remuneration for service to North Shore exceeded \$60,000. Information regarding executive compensation paid by Peoples Gas and its affiliates to Peoples Gas officers is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1986.

### Compensation of Directors

All directors of the Company were officers of the Company who received no compensation for serving as directors.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

### SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

As of November 30, 1986, voting securities of the Company were owned as follows:

<u>Name and Address</u>	<u>Type of Ownership</u>	<u>Number of Shares Owned</u>	<u>Per Cent of Class</u>
<u>Common Stock without par value</u>			
Peoples Energy Corporation 122 South Michigan Avenue Chicago, Illinois 60603	Owned Both of Record and Beneficially	<u>3,625,887</u>	<u>100%</u>
<u>Redeemable Cumulative Preferred Stock, \$100 Par Value</u>			
SAFINSCO Seattle First National Bank Box 12657 Seattle, WA 98111	Owned of Record(a)	8,333	20.8%
National Union Fire Insurance Company 70 Pine Street New York, New York 10270	Owned Both of Record and Beneficially	1,667	4.2%
GMAC Commercial Corporation General Motors Building 3044 West Grand Boulevard Detroit, Michigan 48202	Owned Both of Record and Beneficially	<u>30,000</u>	<u>75.0%</u>
Total		<u>40,000</u>	<u>100%</u>

(a) Beneficially owned by SAFECO Insurance Company of America  
SAFECO Plaza  
Seattle, Washington 98185



ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT (Continued)

SECURITY OWNERSHIP OF MANAGEMENT

No equity securities of the Company are beneficially owned directly or indirectly by any director or officer of the Company.

Information regarding Common Stock, without par value, of Peoples Energy beneficially owned directly or indirectly by directors and executive officers of the Company is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1986.

CHANGES IN CONTROL

None.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

None.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

	<u>Page</u>
(a) 1. Financial Statements:	
See Part II, Item 8.	12
2. Financial Statement Schedules:	
<u>Schedule</u>	
<u>Number</u>	
V Property, Plant and Equipment at Original Cost	34
VI Accumulated Provision for Depreciation of	
Property, Plant and Equipment	36
VIII Valuation and Qualifying Accounts	37
IX Short-Term Borrowings	39
X Supplementary Income Statement Information	40
3. Exhibits:	
See Exhibit Index on page 42.	
(b) Reports on Form 8-K filed during the final quarter of fiscal year 1986:	
None.	

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<u>Fiscal Year Ended September 30, 1986</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,798	\$ 45	\$ --	\$ --	\$ 3,843
Storage plant	6,793	478	--	--	7,271
Distribution plant	108,633	8,922	727	--	116,828
General plant	7,087	1,098	249	--	7,936
Construction work in progress	1,178	214	--	--	1,392
Gas stored underground - Noncurrent	<u>648</u>	<u>53</u>	<u>--</u>	<u>--</u>	<u>701</u>
Total public utility facilities	128,137	10,810	976	--	137,971
Nonutility property	<u>630</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>630</u>
Total property, plant and equipment, at original cost	<u>\$128,767</u>	<u>\$ 10,810</u>	<u>\$ 976</u>	<u>\$ --</u>	<u>\$138,601</u>
<u>Fiscal Year Ended September 30, 1985</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,784	\$ 14	\$ --	\$ --	\$ 3,798
Storage plant	6,254	539	--	--	6,793
Distribution plant	102,830	6,385	582	--	108,633
General plant	6,791	648	352	--	7,087
Construction work in progress	752	426	--	--	1,178
Gas stored underground - Noncurrent	<u>588</u>	<u>60</u>	<u>--</u>	<u>--</u>	<u>648</u>
Total public utility facilities	120,999	8,072	934	--	128,137
Nonutility property	<u>630</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>630</u>
Total property, plant and equipment, at original cost	<u>\$121,629</u>	<u>\$ 8,072</u>	<u>\$ 934</u>	<u>\$ --</u>	<u>\$128,767</u>

North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 2 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<u>Fiscal Year Ended September 30, 1984</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,778	\$ 6	\$ --	\$ --	\$ 3,784
Storage plant	5,675	579	--	--	6,254
Distribution plant	99,327	4,217	776	62	102,830
General plant	6,347	1,175	731	--	6,791
Construction work in progress	557	195	--	--	752
Gas stored underground - Noncurrent	<u>574</u>	<u>14</u>	<u>--</u>	<u>--</u>	<u>588</u>
Total public utility facilities	116,258	6,186	1,507	62	120,999
Nonutility property	<u>630</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>630</u>
Total property, plant and equipment, at original cost	<u>\$116,888</u>	<u>\$ 6,186</u>	<u>\$ 1,507</u>	<u>\$ 62</u>	<u>\$121,629</u>

North Shore Gas Company and Subsidiary Companies

ACCUMULATED PROVISION FOR DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

(000's)

Column A	Column B	Column C		Column D			Column E	Column F
Description	Balance at beginning of period	Additions charged to costs and expenses (a) Depreciation expense	Clearing accounts	Retirement of property at cost	Deduct retirements Cost of dismantling	Stores and miscellaneous (salvage)	Other changes	Balance at end of period
<u>Fiscal Year Ended September 30, 1986</u>								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 2,002	\$ 130	\$ --	\$ --	\$ --	\$ --	\$ --	\$ 2,132
Storage plant	1,562	243	--	--	--	--	--	1,805
Distribution plant	35,733	3,744	--	727	271	(8)	--	38,487
General plant	<u>2,506</u>	<u>226</u>	<u>376</u>	<u>249</u>	<u>13</u>	<u>(29)</u>	<u>--</u>	<u>2,875</u>
Total accumulation provision for depreciation	<u>\$41,803</u>	<u>\$4,343</u>	<u>\$376</u>	<u>\$976</u>	<u>\$284</u>	<u>\$ (37)</u>	<u>\$ --</u>	<u>\$45,299</u>
<u>Fiscal Year Ended September 30, 1985</u>								
Public utility facilities:								
Gas plant in service -								
Production plant	\$ 1,870	\$ 132	\$ --	\$ --	\$ --	\$ --	\$ --	\$ 2,002
Storage plant	1,336	226	--	--	--	--	--	1,562
Distribution plant	32,999	3,539	--	582	245	(12)	10	35,733
General plant	<u>2,272</u>	<u>209</u>	<u>337</u>	<u>352</u>	<u>8</u>	<u>(48)</u>	<u>--</u>	<u>2,506</u>
Total accumulation provision for depreciation	<u>\$38,477</u>	<u>\$4,106</u>	<u>\$337</u>	<u>\$934</u>	<u>\$253</u>	<u>\$ (60)</u>	<u>\$ 10 (b)</u>	<u>\$41,803</u>
<u>Fiscal Year Ended September 30, 1984</u>								
Public utility facilities:								
Gas plant in service (c)	<u>\$35,873</u>	<u>\$3,891</u>	<u>\$267</u>	<u>\$1,507</u>	<u>\$238</u>	<u>\$ (118)</u>	<u>\$ 73 (b)</u>	<u>\$38,477</u>

( ) Denotes red figure.

Notes: (a) Reference is made in Note (1) of the notes to consolidated financial statements with respect to the basis for the provision for depreciation.

(b) Represents the following:

	1985	1984
Accumulated provision for depreciation applicable to property acquired	\$--	\$10
Proceeds from sale of property	10	1
Contributed property which has been retired	--	62
	<u>\$10</u>	<u>\$73</u>

(c) For fiscal year 1984, a segregation of the accumulated provision for depreciation, as set forth in Column A of the related Schedule of Property, Plant and Equipment, at Original Cost (Schedule V), is not available.

North Shore Gas Company and Subsidiary Companies

Schedule VIII  
Page 1 of 2

VALUATION AND QUALIFYING ACCOUNTS  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance</u> <u>at beginning</u> <u>of period</u>	<u>Additions</u> <u>Charged</u> <u>to costs</u> <u>and</u> <u>expenses</u>	<u>Deductions</u> <u>Charges for the</u> <u>purpose for which the</u> <u>reserves or deferred</u> <u>credits were created</u>	<u>Balance</u> <u>at end of</u> <u>period</u>
<u>For Fiscal Year Ended September 30, 1986</u>				
RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 714</u>	<u>\$1,002</u>	<u>\$1,082</u>	<u>\$ 634</u>
RESERVES (not deducted from assets in balance sheet) AND				
DEFERRED CREDITS:				
Injuries and damages	<u>\$ --</u>	<u>\$ 227</u>	<u>\$ 227</u>	<u>\$ --</u>
Pensions	<u>29</u>	<u>59</u>	<u>62</u>	<u>26</u>
Other	<u>739</u>	<u>544</u>	<u>681</u>	<u>602</u>
Total	<u>\$ 768</u>	<u>\$ 830</u>	<u>\$ 970</u>	<u>\$ 628</u>

For Fiscal Year Ended September 30, 1985

RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 662</u>	<u>\$ 786</u>	<u>\$ 734</u>	<u>\$ 714</u>
RESERVES (not deducted from assets in balance sheet) AND				
DEFERRED CREDITS:				
Injuries and damages	<u>\$ --</u>	<u>\$ 33</u>	<u>\$ 33</u>	<u>\$ --</u>
Pensions	<u>32</u>	<u>6</u>	<u>9</u>	<u>29</u>
Other	<u>540</u>	<u>785</u>	<u>586</u>	<u>739</u>
Total	<u>\$ 572</u>	<u>\$ 824</u>	<u>\$ 628</u>	<u>\$ 768</u>

North Shore Gas Company and Subsidiary Companies

Schedule VIII

Page 2 of 2

VALUATION AND QUALIFYING ACCOUNTS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
<u>Description</u>	<u>Balance at beginning of period</u>	<u>Additions Charges to costs and expenses</u>	<u>Deductions Charges for the purpose for which the reserves or deferred credits were created</u>	<u>Balance at end of period</u>
<u>For Fiscal Year Ended September 30, 1984</u>				
RESERVES (deducted from assets in balance sheet):				
Uncollectible items	<u>\$ 561</u>	<u>\$ 590</u>	<u>\$ 489</u>	<u>\$ 662</u>
RESERVES (not deducted from assets in balance sheet) AND DEFERRED CREDITS:				
Injuries and damages	<u>\$ --</u>	<u>\$ 345</u>	<u>\$ 345</u>	<u>\$ --</u>
Pensions	<u>36</u>	<u>5</u>	<u>9</u>	<u>32</u>
Other	<u>531</u>	<u>1,150</u>	<u>1,141</u>	<u>540</u>
Total	<u>\$ 567</u>	<u>\$1,500</u>	<u>\$1,495</u>	<u>\$ 572</u>

Schedule IX

North Shore Gas Company and Subsidiary Companies

SHORT-TERM BORROWINGS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E (a)</u>	<u>Column F (b)</u>
<u>Category of Aggregate</u> <u>Short-Term Borrowings</u>	<u>Balance at</u> <u>End of Period</u>	<u>Weighted</u> <u>Average</u> <u>Interest Rate</u>	<u>Maximum Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Average Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Weighted Average</u> <u>Interest Rate</u> <u>During the Period</u>
<u>Fiscal Year Ended September 30, 1985</u>					
Commercial Paper	\$ --	--	\$5,000	\$ 83	8.31%

- (a) Computed by multiplying the amounts outstanding by the days outstanding and dividing the results by the number of days used in accordance with the loan agreement.
- (b) Computed by dividing the applicable interest expense by the average amount outstanding during the period.

There were no short-term borrowings in fiscal 1986 or 1984.



North Shore Gas Company and Subsidiary CompaniesSUPPLEMENTARY INCOME STATEMENT INFORMATION

Maintenance, depreciation, rents, royalties, advertising costs and research and development costs, other than those specifically disclosed in the Statements of Consolidated Income, are not significant.

Significant taxes, other than taxes on income, including those charged to clearing and other accounts, are summarized as follows:

	<u>Fiscal Years Ended September 30,</u>		
	<u>1986</u>	<u>1985</u>	<u>1984</u>
		(000's)	
Real estate, invested capital, personal property, state capital stock and state franchise	\$ 927	\$ 910	\$ 889
Illinois public utility	6,800	7,394	7,107
Municipal public utility	4,173	4,501	4,364
Social security	614	577	548
Other	<u>311</u>	<u>248</u>	<u>244</u>
Total	<u>\$ 12.825</u>	<u>\$ 13.630</u>	<u>\$ 13.152</u>

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NORTH SHORE GAS COMPANY

Date: December , 1986

By: E. A. TRACY  
E. A. Tracy  
Chairman of the Board and Chief  
Executive Officer

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities indicated on December , 1986.

<u>E. A. TRACY</u> E. A. Tracy	Chairman of the Board and Chief Executive Officer and Director (Principal Executive Officer)
<u>D. G. HOLM</u> D. G. Holm	Vice President, Secretary and Treasurer and Director (Principal Financial Officer)
<u>M. IGASAKI, JR.</u> M. Igasaki, Jr.	Vice President and Director (Principal Accounting Officer)
<u>L. C. BALDACCI, JR.</u> L. C. Baldacci, Jr.	Director
<u>J. B. HASCH</u> J. B. Hasch	Director
<u>J. HINCHLIFF</u> J. Hinchliff	Director
<u>R. E. TERRY</u> R. E. Terry	Director

North Shore Gas Company and Subsidiary Companies

EXHIBIT INDEX

- (a) The exhibits listed below is filed herewith and made a part thereof:

<u>Exhibit Number</u>	<u>Description of Document</u>	<u>Page Number</u>
3-a	Amendment to the Articles of Incorporation of the Registrant from the State of Illinois, dated April 16, 1986.	
3-b	Articles of Incorporation, as last amended.	
3-c	Amendment to the By-Laws of the Registrant, dated March 27, 1986.	
3-d	By-Laws, as last amended.	

- (b) Exhibits listed below have been filed heretofore with the Securities and Exchange Commission pursuant to the Securities Act of 1933, as amended, and/or the Securities Exchange Act of 1934, as amended, and are incorporated herein by reference. The file number and exhibit number of each such exhibit are stated in the description of such exhibits.

<u>Exhibit Number</u>	<u>Description of Document</u>
4-a	Indenture, dated as of April 1, 1955, from the Company to Continental Illinois National Bank and Trust Company of Chicago as Trustee; Third Supplemental Indenture, dated as of December 20, 1963 (North Shore-File No. 2-35965, Exhibit 4-1); Fifth Supplemental Indenture, dated as of February 1, 1970 (File No. 2-35965, Exhibit 4-2); Supplemental Indenture, dated as of October 1, 1973 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-3); Supplemental Indenture, dated as of February 15, 1977 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-4); and Supplemental Indenture, dated as of September 15, 1980 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-5).

---

SECURITIES AND EXCHANGE COMMISSION  
Washington, D.C. 20549

**FORM 10-K**

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF  
THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended September 30, 1985      Commission File Number 2-35965

**NORTH SHORE GAS COMPANY**

(Exact name of registrant as specified in its charter)

**Illinois**

(State or other jurisdiction of  
incorporation or organization)

**36-1558720**

(IRS Employer  
Identification No.)

**122 South Michigan Avenue, Chicago, Illinois**

(Address of principal executive offices)

**60603**

(Zip Code)

**Registrant's telephone number, including area code:**  
**(312) 431-4000**

**Securities registered pursuant to Section 12(b) of the Act:   None**

**Securities registered pursuant to Section 12(g) of the Act:   None**

Indicate by check mark whether the registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X No     

State the aggregate market value of the voting stock held by non-affiliates of the registrant:

Redeemable Cumulative Preferred Stock, \$5,000,000 at November 30, 1985, based on the price at which the stock was sold.

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date:

Common Stock, without par value, 3,625,887 shares outstanding at November 30, 1985.

Documents Incorporated by Reference  
None

## CONTENTS

<u>Item No.</u>		<u>Page No.</u>
	<u>Part I</u>	
1.	Business	3
2.	Properties	8
3.	Legal Proceedings	8
4.	Submission of Matters to a Vote of Security Holders	9
	<u>Part II</u>	
5.	Market for the Company's Common Stock and Related Stockholder Matters	10
6.	Selected Financial Data	10
7.	Management's Discussion and Analysis of Financial Condition and Results of Operations	11
8.	Financial Statements and Supplementary Data	13
9.	Disagreements on Accounting and Financial Disclosure	13
	<u>Part III</u>	
10.	Directors and Executive Officers of the Company	30
11.	Executive Compensation	32
12.	Security Ownership of Certain Beneficial Owners and Management	32
13.	Certain Relationships and Related Transactions	33
	<u>Part IV</u>	
14.	Exhibits, Financial Statement Schedules and Reports on Form 8-K	34
	Signatures	43
	Exhibit Index	44

North Shore Gas Company

ANNUAL REPORT ON FORM 10-K

FISCAL YEAR ENDED SEPTEMBER 30, 1985

PART I

ITEM 1. BUSINESS

GENERAL

North Shore Gas Company (Company) is an operating public utility engaged primarily in the purchase, storage, distribution and sale of natural gas at retail to approximately 101,000 residential, commercial and industrial customers within its service area of approximately 275 square miles, located in northeastern Illinois. It serves 56 communities and adjacent areas, including those situated along Lake Michigan from Winnetka, Illinois to the Illinois-Wisconsin state line. This area, with an estimated population of 385,000, contains residential concentrations and a diversity of industrial and commercial establishments, as well as some farm lands. The Company had 224 employees at September 30, 1985.

The Company holds certificates of public convenience and necessity issued by the Illinois Commerce Commission (Ill. C.C.) for the conduct by the Company of its operations in the territory which it serves. It holds a license agreement from Lake County, Illinois, and, with minor exceptions, franchises from all of the incorporated cities and villages in its service territory. The franchises are of various terms and expiration dates, and are generally subject to various other conditions, restrictions or limitations not deemed materially burdensome.

At September 30, 1985, all of the common stock of the Company and of its affiliate, The Peoples Gas Light and Coke Company (Peoples Gas), was wholly-owned by Peoples Energy Corporation (Peoples Energy). On September 9, 1981, Peoples Energy's common stockholders approved a plan of reorganization which became effective on November 30, 1981. This reorganization resulted in two separate, unaffiliated holding companies - Peoples Energy and MidCon Corp. See Item 3, "Legal Proceedings" for additional information regarding the reorganization.

COMPETITION

Competition in varying degrees exists between natural gas and other fuels or forms of energy available to consumers in the Company's service area. Natural gas prices remained relatively stable during the last year, enabling gas to maintain a definite edge over competitive fuels. Overall, natural gas prices in the Company's service area compared very favorably on a national basis. The possibility of new or improved sources or uses of energy, limitations on future gas supply, changes in relative prices of competing fuels, changes in environmental controls and other factors could, in the future, affect the Company's business. See "Federal Legislation and Regulation".

## ITEM 1. BUSINESS (Continued)

### SALES AND RATES

The Company sells natural gas having an average heating value of approximately 1,000 British thermal units (Btu's) per cubic foot.\* Sales are made and service rendered by the Company pursuant to rate schedules on file with the Ill. C.C. containing various service classifications largely reflecting customers' different uses. Monthly adjustments to the Gas Charge under the Company's rate schedules provide for the pass-through of the increases or decreases in natural gas supplier rates, purchased storage service costs, transportation charges, liquefied petroleum gas costs and purchases of synthetic natural gas (SNG). In addition, under the tariffs of the Company, the difference in any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is recorded either as a current liability or current asset (with a contra to gas costs) and the difference is refunded or recovered over a twelve-month period beginning the following January 1. See Note (3), "Rate Matters" of Notes to Consolidated Financial Statements for more information.

The Company has experienced load losses resulting from economic conditions and conservation efforts by customers. The basic marketing plan of the Company is to retain its strong position in the residential market while seeking expansion of the commercial and industrial markets.

### STATE LEGISLATION AND REGULATION

The Company is subject to the jurisdiction of and regulation by the Ill. C.C., which has general supervisory and regulatory powers over practically all phases of the public utility business in Illinois, including rates and charges, issuance of securities, services and facilities, systems of accounts, investments, safety standards, transactions with affiliated interests, as defined in the Illinois Public Utilities Act, and other matters.

Illinois legislation (Legislation) has been enacted which requires the Ill. C.C. to implement on a three-year trial basis regulations which, in general, will prohibit a utility from discontinuing service to any low-income customer who is eligible for assistance in paying his heating bills under the Illinois Home Energy Assistance Program, provided such customer pays a specified portion of his income to the utility. The Ill. C.C. has implemented the Legislation by emergency rules effective for a 150-day period commencing on December 1, 1985. Under such emergency rules, a qualified low-income customer will not be required to pay a gas utility more than 8% of such customer's income during the winter heating season. The Company may experience a rise in uncollectible accounts in the future due to the Legislation and the Ill. C.C.'s regulations thereunder, but the Company cannot reasonably determine at this time the future impact of this Legislation.

The Ill. C.C. has adopted the federal safety standards established under the Natural Gas Pipeline Safety Act of 1968 and is enforcing such standards with respect to the Company. The Company has a continuing program of inspection designed to keep all of its facilities in compliance with pipeline safety and pollution control requirements. The Company has made a complete inspection of all of its operational facilities and to the best of its knowledge is in substantial compliance with all pipeline safety and pollution control requirements.

---

\* All volumes of natural gas set forth in this report are stated on a 1,000 Btu (per cubic foot) billing basis.

## ITEM 1. BUSINESS (Continued)

### FEDERAL LEGISLATION AND REGULATION

By Order entered on December 6, 1968 (Holding Company Act Release No. 16233), the Securities and Exchange Commission, pursuant to Section 3(a)(1) of the Public Utility Holding Company Act of 1935 (Act) exempted Peoples Energy and its subsidiary companies as such (including the Company) from the provisions of the Act other than Section 9(a)(2) thereof.

The Natural Gas Policy Act (NGPA), a major part of the National Energy Act enacted in 1978, instituted important changes in the laws affecting the natural gas industry. The NGPA (1) established ceiling prices at the wellhead for both interstate and previously unregulated intrastate gas, (2) deregulated the wellhead price of certain "high-cost" gas as of November 1, 1979, (3) deregulated the wellhead price of a major portion of the nation's gas supplies as of January 1, 1985, and (4) will deregulate the wellhead prices of gas in other categories in 1987. No material financial impact has resulted for the Company from NGPA deregulation provisions.

The NGPA also contains incremental pricing provisions which may result in increased rates to certain classes of industrial customers. These regulations are presently effective only for large industrial boilers. The Federal Energy Regulatory Commission (FERC) has, by rulemaking, exempted from incremental pricing all other industrial users which would otherwise be subject to these regulations under the terms of the statute. The Company has not experienced any adverse market effect due to the incremental pricing regulations.

Another part of the National Energy Act, entitled The Power Plant and Industrial Fuel Use Act, prohibits new electric power plants and new major fuel burning installations from using natural gas. Such end use limitations may result in lost market opportunities for the Company.

In late 1985, the FERC issued Orders 436 and 436A which, among other things, offer pipelines an option, effective November 1, 1985, to transport gas on a nondiscriminatory basis for all shippers under expedited regulatory procedures. Pipelines that exercise this option are required, as a condition thereto, to allow firm sales customers to reduce ratably their gas purchases under firm sales contracts or convert their gas purchases to firm transportation service over a five-year period following the pipeline's election to transport gas on a nondiscriminatory basis.

Under the nondiscriminatory transportation program, a participating pipeline may provide transportation service directly to, or for, end-users. Such direct transportation service could have adverse effects on the Company. To date, the Company's supplier has not elected to participate in the nondiscriminatory transportation program. The Company is unable, at this time, to determine whether the FERC orders will have any material effect on its future operations.

### GAS SUPPLY ADVANCES AND INVESTMENTS

During the shortage of the 1970's, the Company undertook several programs to augment its gas supply. Since 1971, the Company, with Ill. C.C. approval, through a pipeline supplier, has made advance payments or equity investments in gas and oil exploration and development ventures. At September 30, 1985, \$1.9 million in advances and equity investments remain outstanding. The Company is allowed by the Ill. C.C. to include such advances and investments in the rate base and treat any profits or losses as utility transactions. See Note (13) of Notes to Consolidated Financial Statements for information on the Company's exploration subsidiary.



ITEM 1. BUSINESS (Continued)

CURRENT GAS SUPPLY

The following tabulation shows the expected peak-day availability of gas in thousand cubic feet (Mcf) during the 1985-86 heating season:

<u>Source</u>	<u>Peak-Day Availability (Mcf)</u>	<u>Year of Contract Expiration</u>
Flow Gas		
Natural.....	135,371	1990 (a)
Peoples Gas (SNG).....	17,000 (b)	1986
Company (LP).....	60,000	
	<u>212,371</u>	
Storage Gas		
Natural.....	101,579 (c)	1986-1995
Peoples Gas (Manlove).....	59,000 (d)	1987
	<u>160,579</u>	
Total expected peak-day availability....	<u>372,950</u>	

- (a) Natural Gas Pipeline Company of America (Natural) may not terminate service at the expiration of service agreements without receiving prior authorization from the FERC.
- (b) The Company has a service agreement with Peoples Gas which provides for the purchase of ten per cent of the production of Peoples Gas' SNG Plant. The plant has a design peak-day production capability of 170,000 Mcf.
- (c) The Company has storage service withdrawals available from Natural of (1) 53,029 Mcf per day subject to maximum seasonal withdrawal of 30 times the maximum daily withdrawal under a service agreement extending to 1990, (2) 6,657 Mcf per day under a service agreement extending to 1992, (3) 4,055 Mcf per day in the peak month, which is January, under a service agreement extending to 1991, (4) 3,412 Mcf per day under a service agreement extending to 1995, (5) 4,426 Mcf per day under a service agreement extending to 1986, and (6) 30,000 Mcf per day under a service agreement extending to 1987.
- (d) The Company has a gas storage agreement with Peoples Gas which provides a maximum withdrawal of 59,000 Mcf of storage service per day. The agreement also makes available "needle peaking" capacity at the discretion of Peoples Gas.

ITEM 1. BUSINESS (Continued)

CURRENT GAS SUPPLY (Continued)

The Company's sources of gas supply and the disposition of that gas in million cubic feet (MMcf) for the three fiscal years ended September 30, 1985, 1984 and 1983 are as follows:

	<u>1985</u>	<u>1984</u>	<u>1983</u>
Source:			
Natural	31,802	33,630	29,945
Peoples Gas - SNG	841	738	953
Liquefied Petroleum Gas Produced	18	48	3
Storage Withdrawals	<u>5,171</u>	<u>5,866</u>	<u>3,428</u>
Total	<u>37,832</u>	<u>40,282</u>	<u>34,329</u>
Disposition:			
Sales	32,022	33,624	30,310
Storage Injections	5,378	5,960	3,601
Company Use, Franchise Requirements and Unaccounted for Gas	<u>432</u>	<u>698</u>	<u>418</u>
Total	<u>37,832</u>	<u>40,282</u>	<u>34,329</u>

## ITEM 2. PROPERTIES

All of the principal plants and properties of the Company have been maintained in the ordinary course of business and are believed to be in satisfactory operating condition. The following is a brief description of the principal plants and operating units of the Company.

The distribution system of the Company, as of September 30, 1985, consists of 1,662 miles of distribution mains and necessary pressure regulators, approximately 93,000 services (pipe connecting the mains with piping on the customers' premises) and approximately 103,000 meters installed on customers' premises. The Company has liquefied petroleum gasification and storage facilities. It also owns and has a substantial investment in office and service buildings, garages, repair shops and motor vehicles, together with the equipment, tools and fixtures necessary to conduct its business.

Most of the principal plants and properties of the Company, other than mains, services, meters, regulators and cushion gas in underground storage, are located on property owned in fee. Substantially all gas mains are installed in public streets, alleys and highways, or under property owned by others under grants of easements. Meters and house regulators in use and a portion of services are located on premises being served.

Substantially all of the physical properties now owned or hereafter acquired by the Company are subject to (a) the direct, first mortgage lien of the Company's Mortgage to the Continental Illinois National Bank and Trust Company of Chicago, Trustee, to secure the principal amount of the Company's First Mortgage Bonds outstanding at September 30, 1985 and (b) in certain cases other exceptions and defects which do not interfere with the use of the property.

## ITEM 3. LEGAL PROCEEDINGS

### Reorganization of Parent and Related Litigation

A reorganization of Peoples Energy approved by the common stockholders and subsequently made effective on November 30, 1981, resulted in two separate, unaffiliated holding companies, Peoples Energy and MidCon Corp. (MidCon). Peoples Energy continued as the parent company for its two gas utilities based in Illinois, Peoples Gas and the Company, while MidCon became the parent for all other companies which were formerly subsidiaries of Peoples Energy.

By order issued November 19, 1982, the Circuit Court of Cook County (Court) declared that the Ill. C.C. has no jurisdiction over Peoples Energy, MidCon, and Natural Gas Pipeline Company of America (Natural), as public utilities, or over Peoples Energy's reorganization. The Court also permanently enjoined the Ill. C.C. from exercising any jurisdiction over Peoples Energy, MidCon, and Natural for the purpose of inquiry into Peoples Energy's reorganization, conducting hearings, or otherwise interfering with Peoples Energy's reorganization. The Court also entered judgment denying all requests for relief sought by the Ill. C.C. and intervenors against Peoples Energy, Peoples Gas, and the Company in this and a companion case brought by the Ill. C.C.

ITEM 3. LEGAL PROCEEDINGS (Continued)

Reorganization of Parent and Related Litigation (Continued)

In December, 1982, the Ill. C.C. and five intervenors filed appeals in the First District Appellate Court of Illinois. It is the opinion of the Company's counsel and trial counsel that the declaratory relief and permanent injunction order is proper and will be upheld in any appellate review.

In May, 1982, the State's Attorney of Cook County, Illinois and the City of Chicago each filed a class-action complaint in the Federal District Court for the Northern District of Illinois against MidCon, Peoples Energy, Peoples Gas, the Company, certain officers and directors of these companies, and Arthur Andersen & Co., Peoples Energy's independent public accountants.

The suits, among other things, allege that the defendants conspired to defraud the customers of Peoples Gas and the Company by diverting revenues received as a result of rate increases granted to such companies during fiscal years 1977 through 1981, to finance, develop, and capitalize MidCon and the entities which are now subsidiaries of MidCon following the November 30, 1981, reorganization of Peoples Energy approved by its shareholders. The plaintiffs allege violations of the Racketeer Influenced and Corrupt Organizations Act (RICO) based on the defendants' purported use of U.S. mail in furtherance of the alleged scheme to defraud. The plaintiffs allege damages in excess of \$100 million and seek, among other relief, the trebling of any damages awarded as is permitted under RICO.

In 1983, the District Court dismissed in their entirety the plaintiffs' suits and in September, 1985, the dismissal was upheld on appellate review. The time for requesting review of the appellate decision has not expired. The Company believes the dismissal order is proper and the Company has no reason to believe that there is any merit to charges that were set forth in the complaints.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

None.

## PART II

### ITEM 5. MARKET FOR THE COMPANY'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The Company is a wholly-owned subsidiary of Peoples Energy.

### ITEM 6. SELECTED FINANCIAL DATA

For fiscal years ended September 30,	1985	1984	1983	1982	1981
<b>OPERATING RESULTS (thousands)</b>					
Operating Revenues:					
Residential	\$ 99,472	\$ 98,818	\$ 85,984	\$ 90,465	\$ 75,789
Commercial	40,837	40,319	35,532	36,325	31,276
Industrial	34,052	32,765	29,845	27,994	29,602
Other	966	1,199	1,374	1,708	1,405
Total Operating Revenues	<u>175,327</u>	<u>173,101</u>	<u>152,735</u>	<u>156,492</u>	<u>138,072</u>
Less - Gas costs	118,789	122,314	108,049	109,629	96,236
- Revenue taxes	12,026	11,598	10,541	11,049	8,050
Net Operating Revenues	<u>\$ 44,512</u>	<u>\$ 39,189</u>	<u>\$ 34,145</u>	<u>\$ 35,814</u>	<u>\$ 33,786</u>
Net Income Applicable to Common Stock	\$ 8,782	\$ 6,847	\$ 4,549	\$ 5,719	\$ 5,485
<b>GAS SALES VOLUMES (million cubic feet)</b>					
Residential	17,209	18,323	16,378	18,777	17,741
Commercial	7,946	8,377	7,563	8,361	8,200
Industrial	6,867	6,924	6,369	6,374	7,623
Total	<u>32,022</u>	<u>33,624</u>	<u>30,310</u>	<u>33,512</u>	<u>33,564</u>
<b>NUMBER OF CUSTOMERS (average)</b>					
Residential	94,393	93,126	92,256	91,769	91,542
Commercial	5,769	5,595	5,487	5,356	5,229
Industrial	700	695	655	631	642
Total	<u>100,862</u>	<u>99,416</u>	<u>98,398</u>	<u>97,756</u>	<u>97,413</u>
<b>DEGREE DAYS</b>					
Per cent of normal (6,455)	103	111	97	112	99
<b>ASSETS (thousands)</b>					
Property, plant and equipment	\$128,767	\$121,629	\$116,888	\$110,993	\$106,842
Less-Accumulated depreciation	<u>41,803</u>	<u>38,477</u>	<u>35,873</u>	<u>32,547</u>	<u>29,301</u>
Net Property, Plant and Equipment	<u>\$ 86,964</u>	<u>\$ 83,152</u>	<u>\$ 81,015</u>	<u>\$ 78,446</u>	<u>\$ 77,541</u>
Capital Expenditures	\$ 8,072	\$ 6,186	\$ 6,480	\$ 4,869	\$ 3,623
Total Assets	<u>\$130,756</u>	<u>\$122,780</u>	<u>\$131,546</u>	<u>\$126,041</u>	<u>\$120,037</u>
<b>CAPITALIZATION AT YEAR END (thousands)</b>					
Common equity	\$ 41,197	\$ 39,086	\$ 37,824	\$ 36,937	\$ 35,279
Preferred stock	4,000	5,000	6,000	7,000	8,000
Long-term debt	<u>33,082</u>	<u>38,494</u>	<u>39,936</u>	<u>41,204</u>	<u>42,710</u>
Total	<u>\$ 78,279</u>	<u>\$ 82,580</u>	<u>\$ 83,760</u>	<u>\$ 85,141</u>	<u>\$ 85,989</u>
<b>CAPITALIZATION RATIOS AT YEAR END (per cent)</b>					
Common equity	53	47	45	43	41
Preferred stock	5	6	7	8	9
Long-term debt	<u>42</u>	<u>47</u>	<u>48</u>	<u>49</u>	<u>50</u>
Total	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>	<u>100</u>

The Company is a wholly-owned subsidiary of Peoples Energy; therefore, cash dividends declared per share and earnings per share are omitted.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION  
AND RESULTS OF OPERATIONS

Results of Operations

Net income applicable to common stock increased by \$1.9 million in 1985 mainly due to a rate increase which became effective in late 1984. This increase was offset, in part, by a reduction in gas sales due to warmer weather than in the prior period. The increase in 1984 was mainly due to weather that was much colder than the previous year, rate changes which became effective in 1983, and increased interest income.

Weather variations affect the volumes of gas sold for heating and, therefore, can have a significant impact on net income. The effect on net income of the major operating cost - that of gas purchased or produced - is mitigated because such costs are recovered from customers through the gas cost recovery provision in the Company's rate schedules. A summary of significant variations in income is presented below with explanations following:

(Thousands of dollars)	Fiscal 1985 Over 1984		Fiscal 1984 Over 1983	
	Amount	%	Amount	%
Net operating revenues*	\$5,323	13.6	\$5,044	14.8
Income taxes	2,383	34.1	2,206	46.1
Other income	(515)	(24.0)	507	31.0
Net Income Applicable to Common Stock	1,935	28.3	2,298	50.5

\* Operating revenues net of gas costs and revenue taxes.

( ) Denotes red figure.

The increase in 1985 net operating revenues resulted mainly from a rate increase which became effective late in 1984, offset in part by weather that was warmer than the previous year. The increase in 1984 was primarily a result of colder weather in 1984 as compared to 1983 and rate changes which became effective in 1983.

The increase in income taxes in both periods reflects changes in pre-tax income.

The decrease in other income in 1985 is mainly due to lower interest rates. The increase in other income 1984 is mainly attributable to increased interest income due to more cash available for short-term investments.

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION  
AND RESULTS OF OPERATIONS (Continued)

Liquidity and Capital Resources

The Company has access to outside capital markets and, together with internal sources of funds, expects to have sufficient resources to meet capital requirements. The Company does not anticipate any changes that would materially alter its present liquidity position.

Due to the seasonal nature of gas sales, a major portion of cash collections occurs between November and April. Because of timing differences in the receipt and disbursement of cash, and the level of construction requirements, the Company may borrow on a short-term basis. Short-term borrowings are either repaid with cash from operations or refinanced on a permanent basis with debt and/or equity, depending on money-market conditions and capital structure considerations.

In early fiscal 1985, Moody's Investors Service upgraded its rating of the Company's bonds from A2 to Aa3 while Standard and Poor's upgraded its rating of the bonds from A+ to AA-.

Additional bonds are issuable, upon Ill. C.C. approval, subject to limitations by certain restrictive provisions of the open-end mortgages and supplements thereto. Short-term cash needs are met through borrowing arrangements with banks and/or the issuance of commercial paper. See Note (10) of Notes to Consolidated Financial Statements.

Capital expenditures for additions, replacements and improvements of the utility plant were \$8 million in 1985, \$6.2 million in 1984 and \$6.5 million in 1983. Total capital expenditures for fiscal 1986 are estimated to be \$10.9 million.

See Note (16) of Notes to Consolidated Financial Statements for an estimate of the effects of inflation on the Company.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

	<u>Page</u>
Report of Independent Public Accountants	14
Statements of Consolidated Income for the fiscal years ended September 30, 1985, 1984 and 1983	15
Statements of Consolidated Retained Earnings for fiscal years ended September 30, 1985, 1984 and 1983	15
Consolidated Balance Sheets as of September 30, 1985 and 1984	16
Consolidated Capitalization Statements as of September 30, 1985 and 1984	17
Consolidated Statements of Changes in Financial Position for the fiscal years ended September 30, 1985, 1984 and 1983	18
Notes to the Consolidated Financial Statements	19
Selected Quarterly Financial Data	29

ITEM 9. DISAGREEMENTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

Not applicable.



REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

To North Shore Gas Company:

We have examined the consolidated balance sheets and capitalization statements of North Shore Gas Company (an Illinois Corporation, hereinafter referred to as the Company and a wholly-owned subsidiary of Peoples Energy Corporation) and subsidiary companies as of September 30, 1985 and 1984, and the related statements of consolidated income, retained earnings and changes in financial position for each of the three fiscal years in the period ended September 30, 1985. Our examinations were made in accordance with generally accepted auditing standards and, accordingly, included such tests of the accounting records and such other auditing procedures as we considered necessary in the circumstances.

In our opinion, the consolidated financial statements referred to above present fairly the financial position of the Company and subsidiary companies as of September 30, 1985 and 1984, and the results of their operations and changes in financial position for each of the three fiscal years in the period ended September 30, 1985, in conformity with generally accepted accounting principles applied on a consistent basis.

Our examinations were made for the purpose of forming an opinion on the basic financial statements taken as a whole. The financial statement schedules listed in Item 14(a)2 are presented for purposes of complying with the Securities and Exchange Commission's rules and regulations under the Securities Exchange Act of 1934 and are not part of the basic financial statements. These schedules have been subjected to the auditing procedures applied in the examinations of the basic financial statements and, in our opinion, fairly state in all material respects the financial data required to be set forth therein in relation to the basic financial statements taken as a whole.

ARTHUR ANDERSEN & CO.

Chicago, Illinois  
November 6, 1985

North Shore Gas Company

STATEMENTS OF CONSOLIDATED INCOME  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	<u>1985</u>	<u>1984</u>	<u>1983</u>
OPERATING REVENUES:			
Gas sales	\$174,361	\$171,902	\$151,361
Other	966	1,199	1,374
Total Operating Revenues	<u>175,327</u>	<u>173,101</u>	<u>152,735</u>
OPERATING EXPENSES:			
Gas costs	118,789	122,314	108,049
Operation	15,258	15,698	14,469
Maintenance	2,106	2,102	2,158
Depreciation	4,106	3,891	3,809
Taxes - Income	9,371	6,988	4,782
- State and local revenue	12,026	11,598	10,541
- Other	1,339	1,325	1,335
Total Operating Expenses	<u>162,995</u>	<u>163,916</u>	<u>145,143</u>
OPERATING INCOME	12,332	9,185	7,592
OTHER INCOME:			
Interest income	1,491	2,051	1,599
Miscellaneous	138	93	38
Total Other Income	<u>1,629</u>	<u>2,144</u>	<u>1,637</u>
GROSS INCOME	13,961	11,329	9,229
INCOME DEDUCTIONS:			
Interest on long-term debt	3,693	3,795	3,908
Other interest	1,005	124	134
Amortization of debt discount and expense	24	24	24
Miscellaneous	--	4	--
Total Income Deductions	<u>4,722</u>	<u>3,947</u>	<u>4,066</u>
NET INCOME	9,239	7,382	5,163
Preferred stock dividends	457	535	614
NET INCOME APPLICABLE TO COMMON STOCK	<u>\$ 8,782</u>	<u>\$ 6,847</u>	<u>\$ 4,549</u>

STATEMENTS OF CONSOLIDATED RETAINED EARNINGS  
(Thousands of Dollars)

	For fiscal years ended September 30,		
	<u>1985</u>	<u>1984</u>	<u>1983</u>
BALANCE AT BEGINNING OF YEAR	\$ 14,329	\$ 13,067	\$ 12,180
Add - Net income	9,239	7,382	5,163
Deduct - Dividends on common stock	6,671	5,585	3,662
- Dividends on preferred stock	457	535	614
BALANCE AT END OF YEAR	<u>\$ 16,440</u>	<u>\$ 14,329</u>	<u>\$ 13,067</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company

CONSOLIDATED BALANCE SHEETS  
(Thousands of Dollars)

	As of September 30,	
	<u>1985</u>	<u>1984</u>
<u>PROPERTIES AND OTHER ASSETS</u>		
<u>CAPITAL INVESTMENTS:</u>		
Property, plant and equipment, at original cost	\$128,767	\$121,629
Less - Accumulated depreciation	<u>41,803</u>	<u>38,477</u>
	86,964	83,152
Gas supply advances and investments	<u>1,850</u>	<u>2,274</u>
TOTAL CAPITAL INVESTMENTS	88,814	85,426
<u>CURRENT ASSETS:</u>		
Cash	1,592	953
Temporary cash investments, at cost, which approximates market value	12,000	8,792
Receivables -		
Customers, net of allowance for uncollectible accounts of \$714 and \$662, respectively	5,455	5,701
Other	115	156
Materials and supplies, at average cost	1,323	1,900
Gas in storage, at last-in, first-out cost	18,956	18,840
Gas costs recoverable through rate adjustments	1,560	267
Prepayments	<u>209</u>	<u>130</u>
TOTAL CURRENT ASSETS	41,210	36,739
DEFERRED CHARGES	<u>732</u>	<u>615</u>
TOTAL PROPERTIES AND OTHER ASSETS	<u>\$130,756</u>	<u>\$122,780</u>
<u>CAPITALIZATION AND LIABILITIES</u>		
CAPITALIZATION (see accompanying statement)	\$ 78,279	\$ 82,580
<u>CURRENT LIABILITIES:</u>		
Accounts payable	9,519	8,041
Dividends payable on common stock	--	2,538
Dividends payable on preferred stock	20	97
Customer deposits	5,173	4,851
Sinking fund payments -		
Long-term debt	4,912	944
Redeemable cumulative preferred stock	1,000	1,000
Accrued taxes	989	(1,001)
Gas sales revenue refundable	10,031	4,791
Accrued interest	<u>367</u>	<u>386</u>
TOTAL CURRENT LIABILITIES	32,011	21,647
<u>RESERVES AND DEFERRED CREDITS:</u>		
Deferred income taxes - primarily accelerated depreciation	14,500	13,083
Investment tax credits being amortized over the average lives of related property	5,198	4,898
Other	<u>768</u>	<u>572</u>
TOTAL RESERVES AND DEFERRED CREDITS	20,466	18,553
CAPITAL COMMITMENTS (note 11)		
TOTAL CAPITALIZATION AND LIABILITIES	<u>\$130,756</u>	<u>\$122,780</u>

The accompanying notes are an integral part of these statements.

( ) Denotes red figure.

North Shore Gas Company  
CONSOLIDATED CAPITALIZATION STATEMENTS  
(Thousands of Dollars)

	<u>As of September 30,</u>	
	<u>1985</u>	<u>1984</u>
COMMON STOCKHOLDER'S EQUITY:		
Common stock, without par value		
Authorized 5,000,000 shares,		
Outstanding 3,625,887 shares	\$ 24,757	\$ 24,757
Retained earnings (see accompanying statement)	<u>16,440</u>	<u>14,329</u>
TOTAL COMMON STOCKHOLDER'S EQUITY	41,197	39,086
REDEEMABLE CUMULATIVE PREFERRED STOCK:		
Exclusive of sinking fund payments, due within one year		
Authorized 210,000 and 220,000 shares, respectively,		
par value \$100		
7-7/8% Series, 10,000 and 20,000 shares		
outstanding, respectively	1,000	2,000
.9% Series, 30,000 shares outstanding	<u>3,000</u>	<u>3,000</u>
TOTAL REDEEMABLE CUMULATIVE PREFERRED STOCK	4,000	5,000
LONG-TERM DEBT:		
Exclusive of sinking fund payments, due within one year		
First Mortgage Bonds -		
5% Series C, due December 1, 1986	1,607	1,742
4.8% Series D, due May 1, 1986	--	2,677
9-1/2% Series E, due February 1, 1995	6,625	6,875
8-3/8% Series F, due October 1, 1998	7,750	8,000
8-3/8% Series G, due February 15, 1992	3,600	4,200
12% Series H, due September 15, 1995	<u>13,500</u>	<u>15,000</u>
TOTAL LONG-TERM DEBT	<u>33,082</u>	<u>38,494</u>
TOTAL CAPITALIZATION	<u>\$ 78,279</u>	<u>\$ 82,580</u>

The accompanying notes are an integral part of these statements.

North Shore Gas Company

CONSOLIDATED STATEMENTS OF CHANGES IN FINANCIAL POSITION  
(Thousands of Dollars)

	For fiscal years ended September 30		
	<u>1985</u>	<u>1984</u>	<u>1983</u>
FUNDS PROVIDED:			
Net income	\$ 9,239	\$ 7,382	\$ 5,163
Add - Principal items not requiring current outlay of funds			
Depreciation	4,106	3,891	3,809
Deferred income taxes - primarily accelerated depreciation	1,353	1,122	1,012
Deferred investment tax credits - net	<u>430</u>	<u>345</u>	<u>383</u>
TOTAL FUNDS PROVIDED FROM OPERATIONS	15,128	12,740	10,367
Other	<u>591</u>	<u>789</u>	<u>656</u>
TOTAL FUNDS PROVIDED	<u>\$15,719</u>	<u>\$13,529</u>	<u>\$11,023</u>
FUNDS APPLIED:			
Capital expenditures - construction	\$ 8,072	\$ 6,186	\$ 6,480
Reduction of:			
Long-term debt	1,444	1,443	1,266
Preferred stock	1,000	1,000	1,000
Dividends on common stock	6,671	5,585	3,662
Dividends on preferred stock	457	535	614
Decrease in working capital	<u>(1,925)</u>	<u>(1,220)</u>	<u>(1,999)</u>
TOTAL FUNDS APPLIED	<u>\$15,719</u>	<u>\$13,529</u>	<u>\$11,023</u>
INCREASE (DECREASE) IN WORKING CAPITAL, EXCLUSIVE OF SINKING FUND PAYMENTS, BY COMPONENT:			
Cash and temporary cash investments	\$ 3,847	\$(9,802)	\$ 1,638
Receivables and payables - net	850	3,682	(5,368)
Gas in storage	116	(146)	—
Rate adjustments refundable or recoverable	(3,947)	2,116	523
Accrued taxes	(1,990)	2,949	795
Customer deposits	(322)	(129)	271
Materials and supplies	(576)	136	9
Other	<u>97</u>	<u>(26)</u>	<u>83</u>
DECREASE IN WORKING CAPITAL	<u>\$(1,925)</u>	<u>\$(1,220)</u>	<u>\$(1,999)</u>

The accompanying notes are an integral part of these statements.

( ) Denotes red figure.

North Shore Gas Company

STATEMENT OF MANAGEMENT

These financial statements were prepared by management, which is responsible for their integrity and objectivity. The statements are in conformity with generally accepted accounting principles and, as such, reflect judgments made by management.

Based upon the Company's accounting and internal control systems, along with ongoing internal audit programs, management believes that the accounting records are reliable for the purpose of preparing financial statements and assets are appropriately safeguarded against loss from unauthorized use.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

(1) SIGNIFICANT ACCOUNTING POLICIES

a. Principles of Consolidation

All subsidiaries of the Company are included in the consolidated financial statements. All significant intercompany transactions have been eliminated in consolidation. Certain items previously reported for years prior to 1985 have been reclassified to conform with current year presentation.

b. Property, Plant and Equipment

Property, plant and equipment is stated at original cost and includes appropriate amounts of payroll taxes, employee-benefit costs, administrative costs and an allowance for funds used during construction.

c. Allowance for Funds Used During Construction

The assumed cost of all funds used to finance substantial and lengthy construction is capitalized as a cost element of Utility Plant, with an offsetting credit to Other Income. Under established regulatory practices, the Company is permitted to include in its rates a fair return on, and the recovery of, these capitalized costs by including them in rate base and in the provision for depreciation.

There was no allowance for funds used during construction in fiscal years 1985, 1984 and 1983.

d. Maintenance and Depreciation

It is the practice of the Company to charge to maintenance the cost of repairs, renewals and improvements amounting to less than retirement units of property. When depreciable property is retired, its original cost is charged to the depreciation reserve.

The provision for depreciation substantially reflects the systematic amortization of the original cost of depreciable property over the estimated useful lives on the straight-line method.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(1) SIGNIFICANT ACCOUNTING POLICIES (Continued)

d. Maintenance and Depreciation (Continued)

Additionally, actual dismantling cost, net of salvage, is included in the provision for depreciation in the month incurred. The amounts provided are designed not only to cover losses due to wear and tear which are not restored by maintenance, but also losses due to obsolescence and inadequacy.

The provision for depreciation, expressed as an annual percentage of the original cost of depreciable property, approximated 3.7%, 3.6% and 3.7% for fiscal years 1985, 1984 and 1983.

e. Recovery of Gas Costs

Under the tariffs of the Company, the difference in any fiscal year between costs recoverable through the Gas Charge and the revenues billed to customers under the Gas Charge is recorded either as a current liability or current asset (with a contra to gas costs) and the difference is refunded or recovered over a twelve-month period beginning the following January 1.

f. Gas in Storage

Storage injections are priced at the fiscal-year average of demand and commodity costs of natural gas and synthetic natural gas (SNG) purchased. Withdrawals from storage are priced under the last-in, first-out (LIFO) method. The estimated current replacement cost of gas in inventory exceeded the last-in, first-out cost by approximately \$37 million and \$36 million at September 30, 1985 and 1984, respectively.

g. Taxes

For federal and Illinois income tax purposes, for periods prior to January 1, 1981, the Company adopted liberalized methods of computing depreciation on property additions after December 31, 1953, and the Asset Depreciation Range (ADR) system on property additions after December 31, 1970. For periods after December 31, 1980, the Company is utilizing the Accelerated Cost Recovery System (ACRS).

Deferred income taxes for the difference between tax depreciation computed on these methods and straight-line depreciation are charged to income and credited to accumulated deferred income taxes. This account is charged when liberalized, ADR, or ACRS tax depreciation becomes less than straight-line depreciation.

The investment tax credits have been deferred and are being amortized through credits to income over the book lives of related property.

At September 30, 1985, there are no timing differences for which deferred income taxes have not been provided.

The preceding deferred-tax and tax-credit accounting conforms with regulations of the Ill. C.C.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(2) PENSION PLANS AND POST RETIREMENT BENEFITS

The Company participates in two defined benefit pension plans covering substantially all employees. Total pension expenses for fiscal years 1985, 1984 and 1983 were \$1.2 million, \$1.1 million and \$1.2 million, respectively.

The Company makes annual contributions to the plans equal to the amounts accrued for pension expenses, including amortization of past service costs over periods varying from 15 to 25 years. Accumulated plan benefit information, as furnished by consulting actuaries, and plan net assets for the Company's pension plans are:

	As of October 1,	
	1984	1983
	(Millions)	
Actuarial present value of accumulated plan benefits:		
Vested	\$14.4	\$12.7
Nonvested	1.4	1.3
	<u>\$15.8</u>	<u>\$14.0</u>
Net assets available for benefits	<u>\$17.7</u>	<u>\$17.1</u>

The assumed rate of return used in determining the actuarial present value of accumulated plan benefits was 6.5 per cent for both 1984 and 1983.

In addition to providing pension benefits, the Company provides certain health care and life insurance benefits for retired employees. Substantially all employees may become eligible for such benefit coverage if they reach retirement age while working for the Company. The costs of providing these benefits, which are unfunded, are expensed on the Company's books when paid and amounted to \$147,000 in fiscal 1985.

(3) RATE MATTERS

In late fiscal 1984, the Ill. C.C. granted the Company a rate increase of \$7.1 million on an annual basis. The Company was allowed a 12.47 per cent rate of return on its original cost rate base which reflects a 15.6 per cent cost of common equity. The new rates became effective in September, 1984.



North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(4) COVENANTS REGARDING RETAINED EARNINGS

The Company's Indenture relating to the First Mortgage Bonds and the Stock Purchase Agreements relating to the Cumulative Preferred Stock contain provisions and covenants restricting the payment of cash dividends and the purchase or redemption of capital stock. At September 30, 1985, such restrictions totaled \$6.2 million out of total retained earnings of \$16.4 million.

(5) TAX MATTERS

Provision for Income Taxes For fiscal years ended September 30,	1985	1984	1983
	(000's)		
Current:			
Federal	\$ 6,554	\$ 4,658	\$ 2,837
State	1,034	863	550
Total current income taxes	<u>7,588</u>	<u>5,521</u>	<u>3,387</u>
Deferred, net - Primarily accelerated depreciation			
Federal	1,181	980	877
State	172	142	135
Total deferred income taxes - Primarily accelerated depreciation	<u>1,353</u>	<u>1,122</u>	<u>1,012</u>
Investment tax credits - net:			
Federal	395	325	383
State	35	20	--
Total investment tax credits - net	<u>430</u>	<u>345</u>	<u>383</u>
Total provision for income taxes	<u>\$ 9,371</u>	<u>\$ 6,988</u>	<u>\$ 4,782</u>
Included in operating expenses as taxes - income	<u>\$ 9,371</u>	<u>\$ 6,988</u>	<u>\$ 4,782</u>

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(5) TAX MATTERS (Continued)

The following is a reconciliation between computed federal income tax expense (statutory rate of 46 per cent times pre-tax income) and the total provision for federal income tax expenses:

For fiscal years ended September 30,	1985		1984		1983	
	Amount	Per Cent	Amount	Per Cent	Amount	Per Cent
	(000's)	of Pre-tax Income	(000's)	of Pre-tax Income	(000's)	of Pre-tax Income
Computed federal income tax expense	\$7,990	46.0	\$6,139	46.0	\$4,260	46.0
Amortization of investment tax credit	(241)	(1.4)	(235)	(1.8)	(216)	(2.3)
Book depreciation over depreciation used in tax provision	78	0.5	60	0.5	55	0.5
Other	<u>303</u>	<u>1.7</u>	<u>(1)</u>	<u>--</u>	<u>(2)</u>	<u>--</u>
Total provision for federal income taxes	<u>\$8,130</u>	<u>46.8</u>	<u>\$5,963</u>	<u>44.7</u>	<u>\$4,097</u>	<u>44.2</u>

( ) Denotes red figure.

Tax returns for 1974 through 1979 have been settled with the Internal Revenue Service resulting in a tax deficiency of approximately \$416,000. The impact on net income is not material since the issues consist of income tax provision timing differences.

Tax returns for 1980 through 1982 have been audited by the Internal Revenue Service and a tax deficiency of approximately \$508,000 has been proposed. Issues are being contested and the potential impact on net income is not material since the issues consist of income tax provision timing differences.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(6) DEFERRED CHARGES

	As of September 30,	
	1985	1984
	(000's)	
Deferred interest on gas sales revenue refundable	\$419	\$315
Debt expense being amortized over the lives of outstanding issues	198	225
Other	115	75
	<u>\$732</u>	<u>\$615</u>

(7) COMMON STOCK

No common stock was issued during the fiscal years 1983 through 1985.

(8) REDEEMABLE CUMULATIVE PREFERRED STOCK

	7.875% Series	9.0% Series
Year of issue	1977	1980
Shares outstanding	20,000(a)	30,000
Involuntary liquidation preference (000's)	\$ 2,000	\$ 3,000
Annual dividends per share	\$ 7.875	\$ 9.00
Redemption options:		
Currently effective redemption price per share	\$100.98	(b)
Redemption price per share decreases annually to issue price by (year)	1986	(b)
Redemption through certain refunding operations not permitted prior to (year)	—	1990

(a) Shares outstanding were reduced by 10,000 during fiscal 1985 to meet sinking fund requirements.

(b) Not currently redeemable at the option of the Company.

(9) SINKING FUND REQUIREMENTS

Sinking fund requirements of preferred stock outstanding at September 30, 1985, are \$1.0 million for fiscal years 1986 and 1987. There are no sinking fund requirements for fiscal years 1988 through 1990.

Sinking fund requirements and maturities of long-term debt outstanding at September 30, 1985, for fiscal years 1986 through 1990 are \$4.9 million for 1986, \$3.7 million for 1987 and \$2.6 million each year for 1988 through 1990.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(10) SHORT-TERM BORROWING AND COMPENSATING BALANCES

Short-term cash needs of the Company are met through bank loans and/or the issuance of commercial paper. The outstanding total amount of these borrowings cannot at any time exceed total bank credit then in effect.

To cover projected short-term credit needs of Peoples Gas and the Company and to support the long-term status of the Adjustable-Rate Mortgage Bonds, Series U, V, and W of Peoples Gas, \$100 million in bank credit through an irrevocable revolving credit agreement with various banks was established to extend through fiscal 1987, of which the Company may borrow up to \$15 million.

Payment for the revolving credit agreement with the banks is through compensating balances and/or fees. There were no legal restrictions on the withdrawal of compensating balances and the amounts maintained during fiscal 1985, after recognizing historical float, were not material.

(11) CAPITAL COMMITMENTS

Total contract and purchase order construction commitments of the Company at September 30, 1985, amounted to approximately \$1.4 million.

(12) ASSETS SUBJECT TO LIEN

The Indenture of Mortgage, dated April 1, 1955, as supplemented, securing the First Mortgage Bonds issued by the Company, constitutes a direct, first mortgage lien on substantially all property owned by the Company.

(13) EXPLORATION SUBSIDIARY

North Shore Exploration Company, a wholly-owned subsidiary of the Company was formed in 1973 to engage, directly or indirectly, in lease acquisition and exploration and development programs. The exploration unit has made investments totalling \$4.1 million and through September 30, 1985, has amortized \$3.1 million. The Company is allowed by the Ill. C.C. to include such investments in its rate base and treat any profits or losses as utility transactions.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(14) TEMPORARY CASH INVESTMENTS

	<u>Maturity</u>	<u>As of September 30,</u>	
		<u>1985</u>	<u>1984</u>
		<u>(000's)</u>	
Eurodollar Deposits	10-01-85	\$12,000	\$ --
Commercial Paper	10-01-84	--	8,792
		<u>\$12,000</u>	<u>\$ 8,792</u>

(15) LEGAL PROCEEDINGS

See Item 3 - "Legal Proceedings".

(16) EFFECT OF CHANGING PRICES (Unaudited)

Consolidated financial statements in this report reflect the historical cost of Company assets. The following two tables were prepared in accordance with the Financial Accounting Standards Board (FASB) requirements relating to changing price information. The tables provide an estimate of the effect of inflation on the Company by presenting selected information on the basis of conventional historical cost and current cost. They should be viewed as estimates of the approximate effect of inflation rather than a precise measure.

Current cost information reflects specific price changes from the date of acquisition of the asset to the present. The Handy-Whitman Index of Public Utility Construction Costs was used to develop specific prices.

Under established regulatory practices, utilities generally are limited to recovery of historical cost of their properties in rates charged to customers. When replacement of productive capacity is made by a utility, resulting in a higher historical cost, that utility can file for recovery of the increased depreciation expense and a return on the higher cost of replacement property. The amount by which operating results are affected is dependent, in part, upon the timeliness and extent of such rate increases and cannot be projected.

During periods of inflation, amounts recovered from customers will have less purchasing power than historical dollars invested. As a result, excess cost of the utility plant - stated in terms of current cost over historical cost - is reflected as an adjustment to net recoverable cost. Part of the loss in purchasing power from amounts invested in utility assets is offset by the use of long-term debt and other fixed-return securities to finance a significant portion of these assets. The securities will be repaid with dollars having less value than those received when the securities were issued.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(16) EFFECT OF CHANGING PRICES (Unaudited) (Continued)

Depreciation expense was developed by applying historical depreciation rates to various property accounts after the accounts were adjusted for specific price changes. Storage gas inventories and gas costs were not repriced because purchased gas costs are recovered dollar-for-dollar through the gas cost recovery process. In accordance with FASB guidelines, income taxes have not been adjusted.

Income Adjusted for the Effect of Changing Prices:

	Current Cost (Millions)
Net income applicable to common stock, as reported	<u>\$ 9</u>
Erosion of net income due to additional depreciation and adjustment to net recoverable costs (a)	(3)
Reduction in economic obligation to repay net amounts owed	1
Specific price changes in excess of general price level changes	<u>1</u>
Net erosion of reported net income	<u>(1)</u>
Net income adjusted for the effect of changing prices (b)	<u>\$ 8</u>

---

( ) Denotes red figure.

(a) At September 30, 1985, the current cost of property, plant and equipment, net of accumulated depreciation, in nominal dollars, was \$217 million.

(b) Reported net income adjusted only for the additional depreciation and adjustment to net recoverable cost would be \$6 million.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(16) EFFECT OF CHANGING PRICES (Unaudited) (Continued)

Five-Year Comparison of Selected Supplementary Financial Data Adjusted for Effects of Changing Prices in Average 1985 Dollars:

	For fiscal years ended September 30,				
	<u>1985</u>	<u>1984</u>	<u>1983</u>	<u>1982</u>	<u>1981</u>
	(Millions)				
Operating revenues - As reported	\$ 175	\$ 173	\$ 153	\$ 157	\$ 138
- In average 1985 dollars	\$ 175	\$ 179	\$ 165	\$ 175	\$ 166

Current Cost Information:

Depreciation expense	\$ 10	\$ 10	\$ 9	\$ 10	\$ 10
Specific price changes in excess of general price level changes	1	3	(1)	3	2
Net income adjusted for all effects of changing prices	8	6	4	5	2
Net assets at year-end	\$ 41	\$ 39	\$ 40	\$ 40	\$ 41

General Information:

Reduction in economic obligation to repay net amounts owed	\$ 1	\$ 2	\$ 1	\$ 2	\$ 4
Average consumer price index	319.4	308.1	296.0	286.0	266.2
Year-end consumer price index	324.5	314.5	301.8	293.3	279.3

( ) Denotes red figure.

North Shore Gas Company

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS (Continued)

(17) SELECTED QUARTERLY FINANCIAL DATA (Unaudited)

	<u>Operating Revenues</u>	<u>Operating Income</u> (000's)	<u>Net Income Applicable to Common Stock</u>
First Quarter			
1985	\$ 47,746	\$ 3,709	\$ 2,575
1984	42,406	2,476	1,667
Second Quarter			
1985	79,818	7,404	6,375
1984	77,764	5,947	5,215
Third Quarter			
1985	31,178	1,538	884
1984	36,416	1,468	1,113
Fourth Quarter			
1985	16,585	(319)	(1,052)
1984	16,515	(706)	(1,148)
Fiscal Year			
1985	175,327	12,332	8,782
1984	173,101	9,185	6,847

---

( ) Denotes red figure.



PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY

IDENTIFICATION OF DIRECTORS

<u>Name, Principal Occupation and Other Directorships</u>	<u>Age at 11-30-85</u>	<u>Company Directorship Since</u>
Louis C. Baldacci, Jr. President of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	60	1976
James Hinchliff Vice President and General Counsel of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas.	45	1985
Donald G. Holm Vice President, Secretary and Treasurer of the Company, Peoples Energy and Peoples Gas; Director of Peoples Gas.	58	1982
Masao Igasaki, Jr. Vice President of the Company and Peoples Gas; Vice President and Controller of Peoples Energy; Director of Peoples Gas.	60	1982
Richard E. Terry Executive Vice President of the Company, Peoples Energy and Peoples Gas; Director of Peoples Energy and Peoples Gas.	48	1982
Eugene A. Tracy Chairman of the Board of the Company, Peoples Energy and Peoples Gas.	57	1978

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE COMPANY (Continued)

IDENTIFICATION OF EXECUTIVE OFFICERS

	<u>Position at November 30, 1985</u>	<u>Age at 11-30-85</u>	<u>Position Held Since</u>
Louis C. Baldacci, Jr.	President	60	1985
Patrick J. Doyle	Vice President	48	1985
J. Bruce Hasch	Executive Vice President	47	1985
James Hinchliff	Vice President and General Counsel	45	1984
Donald G. Holm	Vice President, Secretary and Treasurer	58	1981
Masao Igasaki, Jr.	Vice President	60	1977
John A. Lawrisuk	Vice President	57	1981
Ruel F. Lehman, Jr.	Vice President	62	1975
Michael S. Reeves	Vice President	50	1977
Richard E. Terry	Executive Vice President	48	1984
Eugene A. Tracy	Chairman of the Board	57	1981
Robert M. Wilson	Vice President	60	1981

Directors and executive officers of the Company were elected to serve for a term of one year or until their successors are duly elected and qualified.

There are no family relationships between directors and executive officers of the Company.

All of the directors and executive officers of the Company have been continuously employed by the Company and/or its affiliates in various capacities for at least 10 years.

## ITEM 11. EXECUTIVE COMPENSATION

The executive officers of the Company serve both the Company and its affiliate Peoples Gas. Remuneration is paid by Peoples Gas with appropriate amounts billed to the Company for the time such officers serve North Shore. The Company was billed \$326,823 for the services of these officers during fiscal 1985. No individual executive officer's cash remuneration for service to North Shore exceeded \$60,000. Information regarding executive compensation paid by Peoples Gas and its affiliates to Peoples Gas officers is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1985.

### Compensation of Directors

All directors of the Company were officers of the Company who received no compensation for serving as directors.

## ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

### SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS

As of November 30, 1985, voting securities of the Company were owned as follows:

<u>Name and Address</u>	<u>Type of Ownership</u>	<u>Number of Shares Owned</u>	<u>Per Cent of Class</u>
<u>Common Stock without par value</u>			
Peoples Energy Corporation 122 South Michigan Avenue Chicago, Illinois 60603	Owned Both of Record and Beneficially	<u>3,625,887</u>	<u>100%</u>
<u>Redeemable Cumulative Preferred Stock, \$100 Par Value</u>			
SAFINSCO Seattle First National Bank Box 12657 Seattle, WA 98111	Owned of Record(a)	16,667	33.3%
National Union Fire Insurance Company 70 Pine Street New York, New York 10270	Owned Both of Record and Beneficially	3,333	6.7%
GMAC Commercial Corporation General Motors Building 3044 West Grand Boulevard Detroit, Michigan 48202	Owned Both of Record and Beneficially	<u>30,000</u>	<u>60.0%</u>
Total		<u>50,000</u>	<u>100%</u>

(a) Beneficially owned by SAFECO Insurance Company of America  
SAFECO Plaza  
Seattle, Washington 98185

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT (Continued)

SECURITY OWNERSHIP OF MANAGEMENT

No equity securities of the Company are beneficially owned directly or indirectly by any director or officer of the Company.

Information regarding Common Stock, without par value, of Peoples Energy beneficially owned directly or indirectly by directors and executive officers of the Company is set forth in the Annual Report of Peoples Gas on Form 10-K for the fiscal year ended September 30, 1985.

CHANGES IN CONTROL

None.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

None.

PART IV

ITEM 14. EXHIBITS, FINANCIAL STATEMENT SCHEDULES AND REPORTS ON FORM 8-K

	<u>Page</u>
(a) 1. Financial Statements:	
See Part II, Item 8.	13
2. Financial Statement Schedules:	
Schedule <u>Number</u>	
I           Marketable Securities - Other Investments	35
V           Property, Plant and Equipment at Original Cost	36
VI          Accumulated Provision for Depreciation of Property, Plant and Equipment	38
VIII       Valuation and Qualifying Accounts	39
IX          Short-Term Borrowings	41
X           Supplementary Income Statement Information	42
3. Exhibits:	
See Exhibit Index on page 44.	
(b) Reports on Form 8-K filed during the final quarter of fiscal year 1985:	
None.	

Schedule I

North Shore Gas Company and Subsidiary Companies

MARKETABLE SECURITIES - OTHER INVESTMENTS

(000's)

<u>Name of Issues and title of each issue</u>	<u>Number of shares or units - principal amount of bonds and notes</u>	<u>Cost of each issue</u>	<u>Market value of each issue at balance sheet date</u>	<u>Amount at which each portfolio of equity security issues and each other security issue carried in the balance sheet</u>
<u>Fiscal Year Ended September 30, 1985</u>				
MARKETABLE SECURITIES				
Eurodollar Deposits:				
National Westminster Bank	<u>\$12,000</u>	<u>\$12,000</u>	<u>\$12,000</u>	<u>\$12,000</u>

North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 1 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

Column A Classification	Column B Balance at beginning of period	Column C Additions at cost	Column D Retirements	Column E Transfers between accounts	Column F Balance at end of period
Fiscal Year Ended September 30, 1985					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,784	\$ 14	\$ --	\$ --	\$ 3,798
Storage plant	6,254	539	--	--	6,793
Distribution plant	102,830	6,385	582	--	108,633
General plant	6,791	648	352	--	7,087
Construction work in progress	752	426	--	--	1,178
Gas stored underground - Noncurrent	588	60	--	--	648
Total public utility facilities	120,999	8,072	934	--	128,137
Nonutility property	630	--	--	--	630
Total property, plant and equipment, at original cost	\$121,629	\$ 8,072	\$ 934	\$ --	\$128,762
Fiscal Year Ended September 30, 1984					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,778	\$ 6	\$ --	\$ --	\$ 3,784
Storage plant	5,675	579	--	--	6,254
Distribution plant	99,327	4,217	776	62	102,830
General plant	6,347	1,175	731	--	6,791
Construction work in progress	557	195	--	--	752
Gas stored underground - Noncurrent	574	14	--	--	588
Total public utility facilities	116,258	6,186	1,507	62	120,999
Nonutility property	630	--	--	--	630
Total property, plant and equipment, at original cost	\$116,888	\$ 6,186	\$ 1,507	\$ 62	\$121,629

North Shore Gas Company and Subsidiary Companies

Schedule V  
Page 2 of 2

PROPERTY, PLANT AND EQUIPMENT, AT ORIGINAL COST  
(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>	<u>Column F</u>
<u>Classification</u>	<u>Balance at beginning of period</u>	<u>Additions at cost</u>	<u>Retirements</u>	<u>Transfers between accounts</u>	<u>Balance at end of period</u>
<u>Fiscal Year Ended September 30, 1983</u>					
Public utility facilities:					
Gas plant in service -					
Production plant	\$ 3,762	\$ 16	\$ --	\$ --	\$ 3,778
Storage plant	5,089	586	--	--	5,675
Distribution plant	95,340	4,530	543	--	99,327
General plant	5,353	1,036	42	--	6,347
Construction work in progress	245	312	--	--	557
Gas stored underground - Noncurrent	<u>574</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>574</u>
Total public utility facilities	110,363	6,480	585	--	116,258
Nonutility property	<u>630</u>	<u>--</u>	<u>--</u>	<u>--</u>	<u>630</u>
Total property, plant and equipment, at original cost	<u>\$110,993</u>	<u>\$ 6,480</u>	<u>\$ 585</u>	<u>\$ --</u>	<u>\$116,888</u>



## Schedule VI

## North Shore Gas Company and Subsidiary Companies

## ACCUMULATED PROVISION FOR DEPRECIATION OF PROPERTY, PLANT AND EQUIPMENT

(000's)

Column A	Column B	Column C		Column D			Column E	Column F
Description	Balance at beginning of period	Additions charged to costs and expenses (a)		Deduct retirements			Other changes	Balance at end of period
		Depreciation expense	Clearing accounts	Retirement of property at cost	Cost of dismantling	Stores and miscellaneous (salvage)		
Fiscal Year Ended September 30, 1985								
Public utility facilities:								
Gas plant in service								
Production plant	\$ 1,070	\$ 132	\$ --	\$ --	\$ --	\$ --	\$ --	\$ 2,002
Storage plant	1,336	226	--	--	--	--	--	1,562
Distribution plant	32,999	3,639	--	582	245	(12)	10	35,733
General plant	2,272	209	337	352	8	(48)	--	2,506
Total accumulation provision for depreciation	<u>\$18,477</u>	<u>\$4,106</u>	<u>\$337</u>	<u>\$934</u>	<u>\$253</u>	<u>\$ (60)</u>	<u>\$ 10 (c)</u>	<u>\$41,803</u>
Fiscal Year Ended September 30, 1984								
Public utility facilities:								
Gas plant in service (b)	<u>\$35,873</u>	<u>\$1,891</u>	<u>\$267</u>	<u>\$1,507</u>	<u>\$238</u>	<u>\$ (118)</u>	<u>\$ 73 (c)</u>	<u>\$38,477</u>
Fiscal Year Ended September 30, 1983								
Public utility facilities:								
Gas plant in service (b)	<u>\$32,547</u>	<u>\$1,809</u>	<u>\$305</u>	<u>\$ 585</u>	<u>\$239</u>	<u>\$ (34)</u>	<u>\$ 2 (c)</u>	<u>\$35,873</u>

( ) Denotes red figure.

Notes: (a) Reference is made in Note (1) of the notes to Consolidated Financial Statements with respect to the basis for the provision for depreciation.

(b) For years prior to 1985, a segregation of the accumulated provision for depreciation, as set forth in Column A of the related Schedule of Property, Plant and Equipment, at Original Cost (Schedule VI), is not available.

(c) Represents the following:

	1985	1984	1983
Accumulated provision for depreciation applicable to property acquired	\$--	\$10	\$ 2
Proceeds from sale of property	10	1	--
Contributed property which has been retired	--	62	--
	<u>\$10</u>	<u>\$73</u>	<u>\$ 2</u>

North Shore Gas Company and Subsidiary Companies

Schedule VIII  
Page 1 of 2

VALUATION AND QUALIFYING ACCOUNTS  
(000's)

Column A	Column B	Column C	Column D	Column E
Description	Balance at beginning of period	Additions Charged to costs and expenses	Deductions Charges for the purpose for which the reserves or deferred credits were created	Balance at end of period

For Fiscal Year Ended September 30, 1985

RESERVES (deducted from assets in balance sheet):  
Uncollectible items

\$ 662 \$ 786 \$ 734 \$ 714

RESERVES (not deducted from assets in balance sheet) AND  
DEFERRED CREDITS:

Injuries and damages  
Pensions  
Other

\$ -- \$ 33 \$ 33 \$ --  
32 6 9 29  
540 785 596 739

Total

\$ 572 \$ 824 \$ 628 \$ 768

For Fiscal Year Ended September 30, 1984

RESERVES (deducted from assets in balance sheet):  
Uncollectible items

\$ 561 \$ 590 \$ 482 \$ 662

RESERVES (not deducted from assets in balance sheet) AND  
DEFERRED CREDITS:

Injuries and damages  
Pensions  
Other

\$ -- \$ 345 \$ 345 \$ --  
36 5 9 32  
531 1,150 1,141 540

Total

\$ 567 \$ 1,500 \$ 1,495 \$ 1,572

North Shore Gas Company and Subsidiary Companies

Schedule VIII

Page 2 of 2

VALUATION AND QUALIFYING ACCOUNTS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E</u>
		<u>Additions</u>	<u>Deductions</u>	
	<u>Balance</u>	<u>Charges</u>	<u>Charges for the</u>	<u>Balance</u>
<u>Description</u>	<u>at beginning</u>	<u>to costs</u>	<u>purpose for which the</u>	<u>at end of</u>
	<u>of period</u>	<u>and</u>	<u>reserves or deferred</u>	<u>period</u>
		<u>expenses</u>	<u>credits were created</u>	

For Fiscal Year Ended September 30, 1983

RESERVES (deducted from assets in balance sheet):

Uncollectible items	<u>\$ 446</u>	<u>\$ 649</u>	<u>\$ 534</u>	<u>\$ 561</u>
---------------------	---------------	---------------	---------------	---------------

RESERVES (not deducted from assets in balance sheet) AND

DEFERRED CREDITS:

Injuries and damages	\$ --	\$ 197	\$ 197	\$ --
----------------------	-------	--------	--------	-------

Pensions	41	5	10	36
----------	----	---	----	----

Other	<u>518</u>	<u>1,020</u>	<u>1,007</u>	<u>531</u>
-------	------------	--------------	--------------	------------

Total	<u>\$ 559</u>	<u>\$1,222</u>	<u>\$1,214</u>	<u>\$ 567</u>
-------	---------------	----------------	----------------	---------------

Schedule IX

North Shore Gas Company and Subsidiary Companies

SHORT-TERM BORROWINGS

(000's)

<u>Column A</u>	<u>Column B</u>	<u>Column C</u>	<u>Column D</u>	<u>Column E (a)</u>	<u>Column F (b)</u>
<u>Category of Aggregate</u> <u>Short-Term Borrowings</u>	<u>Balance at</u> <u>End of Period</u>	<u>Weighted</u> <u>Average</u> <u>Interest Rate</u>	<u>Maximum Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Average Amount</u> <u>Outstanding</u> <u>During the Period</u>	<u>Weighted Average</u> <u>Interest Rate</u> <u>During the Period</u>

Fiscal Year Ended September 30, 1985

Commercial Paper	\$ --	--	\$5,000	\$ 83	8.31%
------------------	-------	----	---------	-------	-------

- (a) Computed by multiplying the amounts outstanding by the days outstanding and dividing the results by the number of days used in accordance with the loan agreement.
- (b) Computed by dividing the applicable interest expense by the average amount outstanding during the period.

There were no short-term borrowings in fiscal 1983 or 1984.

North Shore Gas Company and Subsidiary CompaniesSUPPLEMENTARY INCOME STATEMENT INFORMATION

Maintenance, depreciation, rents, royalties, advertising costs and research and development costs, other than those specifically disclosed in the Statements of Consolidated Income, are not significant.

Significant taxes, other than taxes on income, including those charged to clearing and other accounts, are summarized as follows:

	Fiscal Years Ended September 30,		
	<u>1985</u>	<u>1984</u>	<u>1983</u>
		(000's)	
Real estate, invested capital, personal property, state capital stock and state franchise	\$ 910	\$ 889	\$ 906
Illinois public utility	7,394	7,107	6,539
Municipal public utility	4,501	4,364	3,888
Social security	577	548	503
Other	<u>248</u>	<u>244</u>	<u>236</u>
Total	<u>\$ 13,630</u>	<u>\$ 13,152</u>	<u>\$ 12,072</u>

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

NORTH SHORE GAS COMPANY

Date: December 20, 1985

By: E. A. TRACY  
E. A. Tracy  
Chairman of the Board

Pursuant to the requirements of the Securities Exchange Act of 1934, this report has been signed below by the following persons on behalf of the registrant and in the capacities and on the date indicated.

E. A. TRACY	Chairman of the Board and Director (Principal Executive Officer)
E. A. Tracy	

D. G. HOLM	Vice President, Secretary and Treasurer and Director (Principal Financial Officer)
D. G. Holm	

M. IGASAKI, JR.	Vice President and Director (Principal Accounting Officer)
M. Igasaki, Jr.	

December 20, 1985

L. C. BALDACCI, JR.	Director
L. C. Baldacci, Jr.	

J. HINCHLIFF	Director
J. Hinchliff	

R. E. TERRY	Director
R. E. Terry	

North Shore Gas Company and Subsidiary Companies

EXHIBIT INDEX

- (a) The exhibit listed below is filed herewith and made a part thereof:

<u>Exhibit Number</u>	<u>Description of Document</u>	<u>Page Number</u>
3-a	By-laws of the Company as amended September 6, 1985.	45

- (b) Exhibits listed below have been filed heretofore with the Securities and Exchange Commission pursuant to the Securities Act of 1933, as amended, and/or the Securities Exchange Act of 1934, as amended, and are incorporated herein by reference. The file number and exhibit number of each such exhibit are stated in the description of such exhibits.

Exhibit  
Number

Description of Document

- |     |   |
|-----|---|
| 3-b | Corporate Charter, as amended, of the Company from the State of Illinois (File No. 2-29139, Exhibit 3-1).   |
| 3-c | Form L. Statement of Resolution Establishing Series Adopted by Board of Directors, \$100 Cumulative Preferred Stock, 9.0% Series (Form 10-K for the fiscal year ended September 30, 1980).  |
| 4-a | Indenture, dated as of April 1, 1955, from the Company to Continental Illinois National Bank and Trust Company of Chicago as Trustee; First Supplemental Indenture, dated as of July 1, 1957; Second Supplemental Indenture, dated as of December 1, 1961; Third Supplemental Indenture, dated as of December 20, 1963; Fourth Supplemental Indenture, dated as of May 1, 1964 (File No. 2-35965, Exhibit 4-1); and Fifth Supplemental Indenture, dated as of February 1, 1970 (File No. 2-35965, Exhibit 4-2); Supplemental Indenture, dated as of October 1, 1973 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-3); Supplemental Indenture, dated as of February 15, 1977 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-4); and Supplemental Indenture, dated as of September 15, 1980 (Form 10-K for the fiscal year ended September 30, 1980, Exhibit 4-5). |